

## Notable British Trials

The Royal Mail Case

# NOTABLE BRITISH TRIALS SERIES

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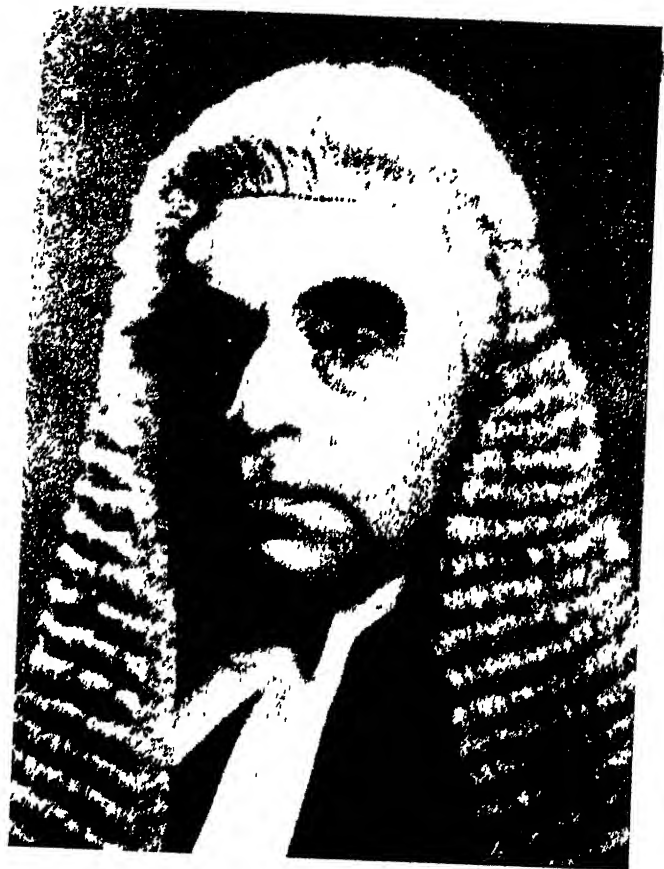
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IN PREPARATION.

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**The Rt. Hon. Lord Wright of Durley, P.C.**  
(Formerly Mr Justice Wright)

# The Royal Mail Case

*Rex v. Lord Kylsant, and Another*

EDITED BY

Collin Brooks

Author of "The Theory and Practice of Finance," "How the Stockmarket Really Works," "Something in The City," "The Tariff Question," &c., &c.

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MADE AND PRINTED IN GREAT BRITAIN  
BY  
WILLIAM HODGE AND COMPANY, LIMITED  
GLASGOW AND EDINBURGH

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*January, 1913*

TO  
THE RIGHT HONOURABLE  
LORD WRIGHT OF DUNLEY, P.C.  
BY HIS PERMISSION  
I DEDICATE THIS VOLUME.



## P R E F A C E .

THE need for a permanent record of the Royal Mail Case is discussed in the Introduction. That need alone would not have brought me to the task of preparing this book, but it was reinforced by the conviction that only such a record will prevent misrepresentation in future years.

The basis of this book is the official shorthand note of the trial, which, before redaction, was compared with various press reports, notably the very full day-to-day account of the proceedings in *The Financial News* and the reports and commentaries in *The Accountant* and the *Journal of the Society of Incorporated Accountants*, to which I would make acknowledgment.

For the opinions expressed in the Introduction I am alone responsible, but I did not enter so contentious a field without seeking, and most readily obtaining, the advice of those more competent than I to discuss the case and its implications. I met, inevitably, a conflict of opinions, and I could not, conscientiously, adopt in every case the advice given to me, although I was grateful for it.

My obligations are many. Chief among them is my debt to the Rt. Hon. Lord Wright of Durley, P.C., who accepted the dedication; the Rt. Hon. Lord Plender, G.B.E., F.C.A.; Sir William McIntock, G.B.E., C.V.O., F.C.A.; Sir William Jowitt, K.C.; Sir Patrick Hastings, K.C.; Mr. Henry Morgan, and Mr. H. J. Morland, F.C.A., all of whom assisted me towards accuracy by reading portions of the proofs, and most of whom gave me valuable other aid. I am indebted also for a courtesy to the Rt. Hon. Sir John Simon, K.C., and especially to Mr. Brian Manning, F.C.A., who was kind enough to read the whole work in proof.

None of these, however, is in any way responsible for the conception, preparation, and form of the book, and my acknowledgments to them are intended only as an expression of personal gratitude for help in a difficult task.

I would assure the friends of Lord Kylsant that special precautions have been taken to avoid in the Introduction the unwitting use of phrases which might seem unjust or unkind, although I may not be specific in describing such precautions. Special care has also been taken to keep the discussion of the significances of the case impersonal.

I must acknowledge a debt to Moodys-Economist Services for certain statistics, and to many financial journalists—chief amongst them Mr. Hargreaves Parkinson of *The Economist*—with whom I have discussed the question of hidden reserves and the probable effect of this case upon the reform of Company Law.

C B

*January, 1933.*

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# THE ROYAL MAIL CASE.

## INTRODUCTION.

THE trial and conviction of Lord Kylsant in 1931 deserve, and even demand, an accessible permanent record for more than one reason. The circumstances and the background of the case gave to it a significance far transcending any temporary interest in the personal tragedy of a distinguished and honourable gentleman who, without criminal intent in the ordinary sense of the term, transgressed the law of the land, and at the age of sixty-eight was committed to gaol after a career of quite remarkable commercial success and public service. Lord Kylsant's offence was, from one viewpoint, so technical as to seem merely the adoption of a practice to which custom had given a certain condonation. From another viewpoint, it was an offence which, however innocently committed, struck deep at the roots of investment confidence and menaced the whole stability of commercial financial practice.

Lord Kylsant was originally charged upon three counts. Upon two of those counts he was acquitted, and upon the third he was found guilty. The Court of Criminal Appeal upheld the verdict. It is quite true to say that the importance of the case would have been little affected had he been acquitted on all three counts. As Mr. Justice Wright was at pains to emphasise in his summing up, the value of the prosecution of the case did not turn upon its success or failure. It turned upon the revelation to the public, and the testing at law, of a state of affairs which permitted a great company, in which the money of the public had been ventured and to which new moneys had been invited, to publish over a period of seven years balance sheets and profit and loss accounts which did not show whether profit had been earned or not, and during those years to pay in dividends the sum of £5,000,000 which had not been found from current earnings, but from non-recurring items of revenue and undisclosed transfers of secret reserves.

Not only had the company, of which Lord Kylsant was the head, issued balance sheets and profit and loss accounts so framed, but in the June of 1928 had invited the public to subscribe for an issue of £2,000,000 of 5 per cent. debenture stock, the prospectus of which stated that the company, although it had suffered from the depression afflicting

## The Royal Mail Case.

the shipping industry, had audited accounts which showed "that during the past ten years the average annual balance available (including profits of the insurance fund), after providing for depreciation and interest on existing debenture stock, has been sufficient to pay the interest on the present issue more than five times over." In addition to this statement the prospectus—which will be found on page 273 of this volume—gave a statement of the dividends paid on the ordinary stock during the preceding fifteen years.

The charge upon which Lord Kysant was actually convicted was that of making, circulating, or publishing a written statement, namely, a prospectus, inviting the public to subscribe to an issue of debenture stock in the Royal Mail Steam Packet Company which he knew to be false in a material particular, in that he concealed the true position of the company, with intent to induce people to entrust or advance property to the said company. But, as was urged during the hearings of the case, the passages in the prospectus contained no statement which could be called false, just as the balance sheets had contained no statements which were actually false.\* The documents had concealed a position, but they had not misstated a position. Upon this point the appeal against the verdict and sentence turned. The Court of Criminal Appeal found that there was ample evidence to justify the finding of the lower Court, and that the falsity consisted in putting before intending investors, as material upon which to base a judgment, figures which appeared to disclose the existing position of the venture and its earnings in which they were invited to participate, but which actually concealed that position.

Lord Kysant was sentenced to be kept in prison in the second division for twelve months

Such, in the very briefest outline, was "the Kysant case." But such an outline itself conceals the real importance and the deep-striking implications of the trial. These only fully emerge from a consideration of the place which was occupied in contemporary financial life by Lord Kysant and the group of shipping companies of which he was the virtual dictator, and for any one to appreciate the place so occupied it is highly necessary that the whole background of world finance be envisaged.

To preserve the prestige of the Royal Mail group of companies, dividends had been paid by the Royal Mail Steam Packet Company—

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\* The many references to the Royal Mail balance sheets in this case were actually references to the profit and loss accounts. This point is emphasised later in the Introduction.

## Introduction.

the parent concern of the group—not from current earnings, but from abnormal sources of profit, not strictly speaking hidden reserves, but so called and treated during the hearing of the case: such “hidden reserves” had been in some cases drawn from subsidiary companies. The method adopted would not have been possible but for the growth of the “group” system of finance. The question immediately arises as to how far the accumulation of hidden reserves is legitimate and what limitations of practice should be imposed upon their use. The secondary question follows as to whether, whatever may be the legal position in regard to the use of such reserves, there is not an obligation upon company directors and company auditors, which is both moral and self-preservatory, to shield the confidence of the investment public from the shock of discovering from time to time that companies apparently enjoying a sufficient current earning capacity are in fact dependent for their dividend policy upon the prosperity of former years which has disappeared and may not return.

If the modern system of “group finance,” with all its administrative advantages, becomes suspect by the investing public of being a system the chief advantage of which is the facility it offers to the controllers of large enterprises to deceive the owners of capital or the potential suppliers of new capital, the whole modern system of capitalising enterprise must suffer. When, by a chain of circumstances shortly to be related, the true financial position of the Royal Mail group was exposed, the system of “group finance” was already known to have been abused. The suspicion was rife that vast aggregations of capital administered through a parent company controlling several subsidiary companies was less justified in the minds of the controllers by the help it gave to the stimulation of industry and the earning of trading profit than by the facility it offered for maintaining in power men who had ceased to be primarily industrialists and had become mere personal money-spinners, their personal position and gain being secured to them as much from the capital providers whose interests they nominally protected as from the customers or users of the enterprises whose needs those enterprises nominally existed to serve.

The growth of limited liability in business finance is familiar to the most superficial student of economic history. To the mid-years of the 19th century the investor of capital in an enterprise literally ventured his personal fortunes. Joint enterprises made their participants not only jointly but severally liable to the full extent of their possessions for the debts of the venture. This risk repelled capital which might otherwise have been attracted. Such heart-rending failures as that of

## The Royal Mail Case.

the City of Glasgow Bank in 1878 definitely checked the progress of commercial enterprise and made difficult the financing of ventures which were of great promise to the economic betterment of the race. But a score of years before the Glasgow failure had demonstrated how easily the fear of personal disaster might dry at the source the flow of investment funds upon which industry depended for its life, there had been incorporated into company law the principle of limited liability, by which the responsibility of any contributor of capital was limited by the amount of contribution represented by the par value of the shares subscribed. Without limitation of liability a participator in an enterprise could be ruined to meet the debts of the venture. with such limitation he was risking only the amount of the share which he had taken. Limited liability had in its application two effects. it widened and strengthened the flow of invested capital, and it often divorced the ownership of capital from its control. As time passed, the shares in enterprises began to change ownership with greater and greater freedom: investors no longer felt the old personal attachment to the industries which they invigorated by their money: investment itself grew less attached to personal knowledge of the personnel of the executive boards controlling businesses: companies were able to attract support more on their records of success than upon the known quality of the contemporary management.

Under the operation of limited liability, stock market business rapidly expanded. Companies increased in number and their nominal ownership, attached to stock or shares, changed often and easily. For one enterprise to acquire another ceased in every case to be a matter of personal negotiation between two owners, and became a matter of stock-market operations, whereby voting power was bought in blocks of shares. The ease whereby control could thus be bought against the will of the existing management led in its turn to companies being capitalised in such a way that control lay not with a majority of the shares, but with a special group of shares which might represent only a minor proportion of the total capitalisation. This, again, led to an exchange of control being possible against the wish, or even without the knowledge, of the great bulk of the nominal proprietors of the enterprise.

While this development in the technique of company finance was proceeding, the technique of production and distribution of commodities was making equal progress. The scope of industry and business was widening, markets and sources of raw material were expanding, methods of conquering time and space were multiplying, to such an extent that the prosperous enterprises had to be large and of a large capitalisation.

## Introduction.

The temptation to a capable man was no longer to grow in commercial power by fighting to the death his competitors until he drove them from business, but to effect with them combinations and mergers.

Into large and successful businesses investors poured their money, and the few men who controlled that money tended to become more and more remote from its owners. At best they were glimpsed once a year at annual meetings: at worst they were never seen and were known only by repute and judged only by the amount of return which, by their efforts, the company they governed could show on an investment in it. The speculative investor was in and out of possession of shares in a company very often within periods of weeks or even days. Men were in and out of control of companies in relatively short periods, where, in one previous generation, such a control would have been a life's devotion.

The effects of this instability of attachment, and this new remoteness of the governing figures from the other units of an enterprise, were more quickly realised by the providers of labour than by the providers of capital. The grouping of enterprises under a single control caused organised Labour some uneasiness, as it had at times caused uneasiness to the consumers who were served by the grouped enterprises; but, for as long as things went well and dividends were forthcoming, it caused no uneasiness to the investors. Small mushroom companies might be unsound and might be manipulated by rogues to trap fools, but large aggregations of capital under one set of hands applied to a number of affiliated and associated companies working in some kind of common purpose were felt to be safer, rather than less safe, than would have been the original units working alone.

After the war, when industry was stimulated by a short-lived boom and stock markets were more than ever before divorced from the immediate actual values behind the scrip that was bought and sold, the investment public expanded rapidly. It is possible that the education of the small saver into the habit of holding War Loan, that is of holding paper securities instead of retaining wealth in more tangible or apparently accessible form, swelled the mass which was eager to increase its possessions by investment or speculation in company shares. The industrial boom ended, but the stock markets in 1928 swelled into a boom of their own for which it is hard to find a parallel other than that of the famous South Sea Bubble days. With such a boom to help them, financiers of little experience and of doubtful morality found it easy to attract subscriptions to their enterprises and were not slow to realise the advantages which arose from manipulating, not a single company,



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but a group of companies. A "parent" company with a number of subsidiaries at its command could do much to baffle the public as to its true state of prosperity. Not only could loans to, and investments in, subsidiaries be so manipulated that balance sheets concealed the true position of the whole group, but sales of rights could be so arranged that a subsidiary could show and transfer a dividend to the parent company which to the average investor may not have been indistinguishable from a true trading profit.

The state of company finance had so far attracted the attention of legislators that a new Companies Act was framed and was expected to become law in 1928. It had, in the event, to be transformed into the Act of 1929. Pending the passing of the Bill into law, every advantage was taken by adventurers of the wide scope allowed to them by the earlier legislation. While the stock-market boom was still swelling, a Mr Brandreth, who had manipulated a group of companies formed to make and market the "Ner-sag Mattress," transgressed the then state of the law; his small group of companies was discovered to be thoroughly unsound; and many guileless investors found themselves heavily hit, if not ruined. The modern "group finance" might have survived this blow, but it was quickly followed by what promised to be, before the Kreuger débâcle, the greatest "crash" of the last two centuries—the fall of the Hatry group of companies and the exposure of their head as a man who had been driven by vanity and ambition, not only into unsound finance, but into actual fraud.

It is not possible, even yet, to estimate the range of the damage done by the Hatry collapse. Its immediate effect was to disorganise the stock markets. Nobody knew which of the shares of the Hatry group and which of the securities which that group had handled were "good" security and which were forgeries. Everybody knew that those investors or speculators or dealers who had been badly hit by the Hatry collapse would have to sell their non-Hatry holdings to meet their commitments. In the case of the Hatry group securities themselves, dealings were suspended and settlement postponed. Other shares were almost indiscriminately marked down to low prices to discourage panic sales. The Stock Exchange, which had seemed to so many people a kind of authorised casino where money was easily to be made, seemed now a dangerous assembly where money could too easily be lost.

Clarence Hatry, unfortunately, stood in the public mind as an exponent and exploiter of the modern method of "group" finance. His fall caused a change in general opinion towards large financial entities comprising a parent and several subsidiary and associated com-

## Introduction.

panies. Even if those critics who held that too large a conglomeration of enterprises and interests under unified control must mean a certain economic weakness and a faulty relationship between management, capital, and labour, were wrong, the critics who held that large groups meant too many opportunities for concealing either ineptitude or misfortune were obviously right.

But even in the distrust of group finance which swelled with the Hatry catastrophe most people of ordinary knowledge and perspicacity felt that the danger of the system was relative. What might be a menace in the hands of untried and unknown controllers, was an assurance in hands that were experienced and known. What might be unsound because new and of too rapid a growth was sound enough when it was old and of gradual growth. There were so many groups of industrial companies which, by the slow process of years of increasing efficiency, and under the pressure of the need for larger and larger amounts of capital to exploit wider and wider markets with more and more expensive plants, owed their standing and undoubted prosperity to the very system which Hatry had brought to such disrepute. Most of these large groups were household names, with a shareholding proprietorship spread through all classes of the community, and with their control vested in men whose own names were synonyms for industrial and financial skill and personal probity. Among these large groups was the Royal Mail Steam Packet Company.

The Royal Mail Steam Packet Company, as any one consulting a standard reference such as Moodys-Economist Services could discover, had been incorporated by Royal Charter on 26th September, 1839. It had successfully weathered the vicissitudes and triumphantly shared the fortunes of the most inspiring and romantic years of British shipping enterprise. In 1851, 1882, 1904, 1912, and 1920 its powers had been increased by further Royal Charters. It owned some 39 vessels and tugs and launches, &c., of a gross registered tonnage of 331,418, including the fleet of R.M.S.P. Meat Transports. It held a controlling interest in the Pacific Steam Navigation Company, Ltd.; the Nelson Steam Navigation Company, Ltd.; MacAndrew's Company, Ltd.; David M'Iver Company, Ltd.; and the White Star Line, Ltd. The combined fleets of these companies totalled 2,635,788 gross registered tonnage.

The names of the gentlemen composing the board of directors were impressive. Lord Kysant, as chairman, had among his colleagues the Duke of Abercorn, Mr. A. N. Lubbock, Sir Leslie Scott, and Lord Suffield.

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The company had an authorised capital of £25,000,000, of which £8,800,000 was issued and paid up in the following categories.—

5 per cent. Non-Cumulative Preference Stock, -	£900,000
6½ per cent. Cumulative Preference Stock, -	£2,900,000
Ordinary Stock, - - - - -	£5,000,000

The preference stocks had priority for capital and dividends without further participation. The voting power was allotted in one vote per £100 ordinary stock or £5 preference stock, the preference stockholders voting only on matters affecting their rights.

The debenture obligation of the company was—

	Authorised.	Issued.	Outstanding.
(a) 4½ per cent. 1st Debenture Stock.	Two-thirds paid-up capital.	£1,400,000	£1,400,000
(b) 5 per cent. Debenture Stock.	Must not exceed paid-up capital.	£5,500,000	£5,100,000

(a) Secured by trust deeds as first floating charge on all assets; no prior charge to be created on company's ships. Redeemable at par at any time on six months' notice from company.

(b) Secured by trust deeds as second floating charge on all assets. Redeemable at par at any time on six months' notice from company.

The company, under the Trade Facilities and Loans Guarantee Acts, also had loans of £2,550,000 to R.M.S.P. Meat Transports, Ltd., guaranteed by the Royal Mail Steam Packet Company itself. These were due for repayment in the September of 1930.

The profit figures, after crediting excess reserve for income tax required in each year, amounts not given, and for the years 1921 to 1928 after fleet depreciation, read thus in the Moodys-Economist analysis—

Year to 31st December.	Profit.
1921,	£710,935
1922,	771,752
1923,	819,441
1924,	811,033
1925,	769,148
1926,	478,536
1927,	737,293
1928,	729,367
1929,	657,149

## Introduction.

Although it was generally realised by the investing public that shipping since the war years had suffered a severe decline in prosperity, the Royal Mail group, with its ancient standing, its large capitalisation, and its famous and trusted chairman, was regarded as a concern in which every confidence could be placed. The more expert observers, who were themselves in shipping or in close touch with the stock markets, felt, perhaps, a little uneasy as to the capacity of the group to maintain its record of profits, but none doubted the integrity of its management. When, therefore, it was known in May, 1931, that summonses had been issued against Lord Kylsant and against the auditor of the Royal Mail Steam Packet Company, there was widespread consternation. At the first hearing of the case against the two defendants at the Guildhall it was announced that not only were the defendants summonsed with regard to the balance sheets of the company, but that a third summons had been made against Lord Kylsant with regard to a prospectus. The case against him assumed immediately in the public mind a more serious aspect.

Although from the opening of the case at the Guildhall to the finding of the Court of Criminal Appeal the hearings teemed with legal and financial technicalities, the core of the case was simple. It was that Lord Kylsant had used his virtually dictatorial powers to have issued by the company balance sheets and a prospectus which misled the public, and that the auditor to the company had, with regard to the balance sheets, connived at—or, in the legal phraseology, “did aid, abet, counsel, procure, or command”—the deception. The professional standing and high personal repute of the auditor, who was acquitted, served still further to unsettle the public mind, since it was felt that if a company of such reputation could issue balance sheets certified by a man of such standing which misled those who read them, there could be no assurance that any limited liability company was being frank with its shareholders and potential shareholders. By a paradox the case assumed a greater importance from the fact that the men charged were not felt to be rogues but honest men.

What had caused the summonses to be issued? To what extent were the charges mere technicalities? What motive could there have been for a wilful deception? What extent of insolvency had been concealed by the misleading documents? These were the questions which agitated the investors and the public.

The first of these questions was quickly answered. In 1929 the R.M.S.P. group had asked that certain assistance received from the Government under the terms of the Trade Facilities Act, 1921, should be

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extended That Act came to an end in March, 1927, leaving in existence certain guarantees which had been undertaken. The chairman of the Trade Facilities Act Advisory Committee from February, 1925, had been Lord Plender, an eminent chartered accountant, who had served on the Committee since its inception. After the termination of the Act he was still called upon by the Treasury to advise with regard to these existing commitments. The loans to the R.M.S.P. group fell due for repayment in 1929 and 1930, and Lord Plender and the Treasury were seen by Lord Kylsant as to the possibility of a postponement of the dates of maturity. For the guidance of the Treasury certain statements were supplied by the auditors of the company. As the Treasury had not the facilities, nor Lord Plender the time, to make a detailed examination of the position of the company, it was decided that some independent person should investigate matters and make a report. For this purpose there was chosen Sir William M'Lintock, of Thomson M'Lintock & Co., chartered accountants, who was selected, in Lord Plender's own words, given in evidence on subpoena, "because of his known competency, his position in the profession, and his impartiality." When Lord Kylsant was informed that Sir William M'Lintock had been selected to examine the position of the company, he immediately proffered every facility. Sir William stipulated that he should have "a free hand" in his examination, and that free hand was not denied to him.

After a long investigation Sir William M'Lintock submitted a report. Upon this report no immediate action was taken, but on 12th February, 1931, at a meeting of the debenture-holders of the Royal Mail Steam Packet Company, a question was asked, to which Sir William replied on behalf of the voting trustees, to the effect that the Royal Mail, while it had paid dividends for several years, had not earned any trading profits. The matter became the subject of a series of questions in the House of Commons, and as a result the Attorney-General undertook to inquire into the matter.\* The charges were then made by the Crown, to answer which the defendants were called to the Guildhall on 2nd June, 1931.

In simple language the charges referring to the balance sheets amounted to this: that in 1926 and 1927 by the profit and loss accounts and the balance sheets, for the form of which Lord Kylsant, as chairman, was responsible, the public was led to believe that the R.M.S.P. group

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\* It may, perhaps, be pointed out that in a case of this nature, the Attorney-General, in deciding to start a prosecution, would submit the papers to distinguished counsel and would be entirely guided by their opinion as to the course he ought to adopt.

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had in those two years made large trading profits whereas in fact the group had made serious losses, and that the auditor to the company, knowing perfectly well what had been done, had condoned the deception and signed the report at the foot of each balance sheet, stating that a true and correct view of the state of the company's affairs as shown by the books of the company had been given. The charge referring to the prospectus was not in substance dissimilar. It was that the document contained a false statement with regard to the issue of debenture stock and was intended to induce persons to entrust or advance property, including money, to the company. The prospectus stated—

Although this company in common with other shipping companies, has suffered from the depression in the shipping industry, the audited accounts of the company show that during the past ten years the average balance available, including the profits of the insurance fund, after providing for depreciation and interest on existing stock, has been sufficient to pay interest on the present issue more than five times over.

The case for the Crown was that the average figures given would be taken to represent a fair criterion of current earning capacity, and that, for reasons given, they were in fact no criterion at all.

In the event, as has been stated above, the charges referring to the balance sheets resulted in the acquittal of the two defendants. On the charge referring to the prospectus, the auditor was not included or, indeed, concerned. But, although the defendants were acquitted on the balance sheet charges, it is legitimate and permissible to ask how such charges could have been framed, by what means a company could issue statements bearing the feasible construction that trading profits had been made when actually trading losses had been incurred.

It is necessary first to remember two points about company reports and balance sheets. One is that a balance sheet can never be more than a picture of the financial state of a concern at a given time. It may assist the trained and intelligent reader to deduce the progress of the company between the issue of one report and the next, but as a thing-in-itself it is but an instantaneous picture of the books of the company at a given date. The second point to remember is that Company Law, even after the Act of 1929 and more so before that year, gives a wide latitude as to how a balance sheet shall be prepared and what it shall contain.

A company in years of prosperity makes profits. Those profits can be, and are, allocated to a variety of purposes. Part of them

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will go to the stockholders or shareholders in the form of dividends. Part will go to special funds, such as staff pension funds or building funds. Part will go to reserve. Part will be "carried forward." Profits which go into reserve are as legitimately the property of the stockholders, who are the proprietors of the company, as are the profits which are distributed in dividends. In theory, sooner or later, those reserve funds will be distributed. It is, obviously, only elementary wisdom to accumulate reserves against misfortune or to provide against needed expenditure forced upon a company by changing methods and times. The plant and machinery and other assets by which the company earns its profits must in time depreciate in value and may need complete replacement. Investments may suffer sudden and unexpected falls in value. For these and similar contingencies reserves must be accumulated. These reserves are shown on a balance sheet in different ways. To take the simplest and most familiar example, a piece of machinery may be shown on one side of a balance sheet at its cost price with an amount shown on the other side of the sheet for its depreciation, or it may be shown on one side of the sheet at a value which represents its cost less such an amount for depreciation. Again, all reserve funds may be lumped into a single reserve or they may be shown in different categories, as "depreciation reserve," "dividend equalisation fund," and so on. Prudence demands that a reserve fund shall be accumulated, but taste, habit, or tradition may dictate varying forms of presenting to the public which reads the balance sheet the fact that a reserve exists and that it is of a certain amount.

In addition to its published reserve, a company of any strength and age tends to accumulate what are known as hidden reserves. If, for example, the head of a banking company writes down in his balance sheet his gilt-edged investments whenever the market at the date of a balance sheet shows a fallen price, but never writes those investments up when the market recovers, he will have at any time of favourable markets a reserve which the balance sheet is not obliged to display. If he and his departmental heads have been in the habit over a period of years of writing down the value of assets and of goodwill, as a measure of reasonable prudence, the difference between the actual marketable value of these things and the value placed upon them in the balance sheet will constitute a hidden reserve of possibly great value.

In the accumulation of such hidden reserves there is nothing legally or morally wrong. Their existence is perfectly proper, and may be highly commendable. But one point of public interest, forced into general consideration by the Kysant case, is how far the conceal-

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ment from the shareholders and potential shareholders of a company of such hidden reserves is proper, and to what purposes can such reserves be applied, without the knowledge of the stockholders or shareholders, without the boundary of honesty being transgressed.

In opening the case for the Crown in the first Court, counsel (Mr. Pritt), after reading a number of extracts from the report and accounts for 1926, referred to the credit side of the account and said,

Then come the words on which a very great deal turns. They are : " Balance for the year, including dividends on shares in allied and other companies, adjustment of taxation, reserves, less depreciation on fleet, &c, £439,212 12s. 1d." There are two minor items which are, in fact, profits, and then comes the phrase : " transfer from reserve fund, £150,000 " The submission for the Crown is that the words beginning " Balance for the year " coupled with the words " transfer from reserve " are a clear representation to the shareholders that the company had earned in that year on its trading £439,000 odd, subject to some modest matter of adjustment of some taxation reserves, and that the transfers from reserves amounted to £150,000 in all. The facts were that the balance of £439,000 was only brought about by wholesale transfers from hidden reserves which had nothing whatever to do with that year at all, and, in fact, had become free a couple of years before . . .

It may be well at this point to emphasise a distinction of viewpoint which, doubtless, affected the verdict of the jury upon the balance sheet charges. The Crown contended that such items in the report and accounts as that just quoted constituted " a deliberate false representation to the shareholders that the company was making a trading profit when in fact it was making a trading loss." There can be little question that the balance sheets were in this respect misleading. How far the directors of the company erred in not telling their shareholders that the company was being kept alive by other than current earnings is one point: how far the deception arising from the mode of presenting the report and accounts was deliberate is another point. Mr. Justice Wright, in his summing up, said of the balance sheets,

. . . of course it is obvious to all of us that if it becomes known to the world that balance sheets of companies are not things which can be relied on, that is a very serious matter for the national affairs and commercial affairs of this country. But, as I have already pointed out, these general considerations are not of value to you in determining the specific question, namely, whether there was a misleading balance sheet; and if misleading, was it misleading to the knowledge and realisation of Lord Kylsant; and if that knowledge and understanding was present to his mind did he then publish it with the fraudulent, wicked, and criminal intent, which the law requires to constitute the offence? Matters of intent are matters which juries have to determine in every action of this character. The charge is a charge of fraud, fraudulent



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intent, and in a sense it can only be decided by a jury as a matter of inference from a consideration of all the relevant circumstances. So far as the other evidence is concerned, those are the relevant facts which have occurred to me, others may occur to you, for consideration. I do not know how far it is in any way definite or tangible at all in this connection, but you have the fact that if the dividend was 5 per cent, certain remuneration became due to Lord Kylsant under his agreement and was in fact collected by him in 1927. It was not collected by him in 1926 because it was not due, because the dividend was only 4 per cent, and in 1928 he did not collect it, though it was passed by the accountants. There is that circumstance which is quite within your knowledge, and it is for you to determine what, if any, weight you should give to this matter.

In considering intent, it is always a question which juries consider in connection with possible motives. Without entering into any fine analysis, it is quite obvious that motive and intent are two different things. A man may have an intent for which no assignable motive can be given. On the other hand, a man may have assignable motives and yet he may not have the intent. One knows in these days of large commercial combinations the leaders of commerce, who are in positions of importance, may sometimes think of the affairs of the company rather in terms of the group, as it is called, than of the company itself. That *prima facie* is an evil, because, after all, however many companies may be associated in a group, and however much they may be under the control of one man or of a body of men, still the primary duty in law is as between the board or the directors and the shareholders of that particular concern, the people who have invested money in that concern. So that if you are looking at motives, the motives may be of a somewhat complex character. It may be the motive that the chairman of a concern may feel that he ought to keep the flag of his company flying until a certain stage is arrived at, when the flag must be lowered, or to change the metaphor, in the old sailing-ship days the captain of a ship may carry on full sail because he is anxious to reach his destination and may overstep the mark and lose either his sails or his masts or both. The question of motive, therefore, in a case of this sort may be of a very complicated character, and you must, as well as you can, weigh all these considerations, because, as I say, intent is a matter of inference from all the facts and circumstances of the case.

The jury, as we know, later absolved Lord Kylsant from any wrong intent in preparing and publishing the balance sheets. They did not deny by their action the contention of the Crown that the sheets were misleading, inasmuch as that hidden reserves had been drawn from subsidiary companies to give to the Royal Mail Steam Packet Company balance sheet an appearance of prosperous trading which was not justified by the trading facts, and that the indication given on the sheets that this had been done was insufficient to acquaint the ordinary person with the action that had been taken.

It will be realised that the verdict on the charges relating to the balance sheets makes a full discussion of the case a matter of delicacy, if not of danger. The Court held that neither Lord Kylsant nor the auditor to the company was guilty of an offence against the law in

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preparing, presenting, and certifying a balance sheet of the peculiar form used; but that form of balance sheet was without question capable of misleading those who read it as to the company's trading position. The inference is that if the two gentlemen who were put on their defence were not wrong in what they had done, the law which permitted the use of that form of balance sheet was itself wrong. The auditor, Mr. Harold John Morland, who was, as has been stated, a man of the highest integrity, of high personal and professional repute, had faithfully fulfilled all that the law had required of him, and in the year 1925 had insisted upon having added to the accounts the words "Adjustment of taxation reserves" in describing the balance for the year. He remained frankly "very much puzzled" to know what he had done that could be considered wrong. Having taken scrupulous professional care to meet all legal requirements, and having been careful to add to the accounts before passing them "as being properly drawn up so as to exhibit a true and correct view of the company's affairs as shown by the books of the company" a reservation which to him, professionally, seemed to imply, if not to state, what had been done to reach the "balance for the year," he yet found himself charged with a very serious offence.

The action of Mr. Morland was approved from the witness-box by the presidents of the Institute of Chartered Accountants and the Society of Incorporated Accountants and Auditors, and by Mr. Brian Manning, chartered accountant, called as an expert witness. Mr. Morland, moreover, was a member of one of the largest firms of accountants in the world, and a man in such a position was obviously unlikely to have yielded to undue influence. He had made a proposal which had been accepted by Lord Kylsant, and this proposal seemed to him, in his long experience, to go as far as any auditor would conceive it to be his duty to go in relation to a profit and loss account.

[It must be noted here that the case for the Crown was put as a matter of degree, and it was expressly stated that no prosecution would ever have been launched had not the utilisations of undisclosed reserves amounted to a very large amount, extending over a large series of years. The case proceeded upon the assumption that the building up and subsequent utilisation of secret reserves without disclosure was not a matter of which complaint could be made, except in special circumstances. In opening the case Sir William Jowitt said:—"If it be said—and said it may be—'Well, but if once you admit that you have to draw a line, it is terribly difficult to know where exactly you are going to draw it,' I think I would say this, 'It is always difficult

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to know where a line has to be drawn; but notwithstanding that you can very easily tell whether a case is one side of the line or the other.' ” It will be realised what a weight of responsibility is thrown upon an auditor by this question of degree and the necessity for deciding upon which side of an undefined line a specific case falls.]

It was the revelation that a balance sheet might be drawn with all legal rectitude and yet the profit and loss account might mislead shareholders that gave to the Kysant case its first importance, so far as the public was concerned. It was the revelation that an auditor could fulfil with care the duty imposed upon him by the law and yet be party to such a document that made the case of special importance to the accountancy profession.

The auditor to a company is not—in theory—the servant of the board of directors: he is the watch-dog of the shareholders. What power he has to influence the form which a company's accounts shall take is debateable. A strong auditor, either by his powers of persuasion or by an appeal to the full board, may prevent the directors from attempting to issue a sheet which is inadequate to the purpose certified at its foot, that of giving a true and correct view of the company's affairs at a given date. A weak auditor, to whom fees or patronage may be of great importance, can construe his duties to the shareholders in the narrowest way, and so become a party to deception, even though that deception be so negative that the law refuses to recognise it as culpable.

The clue to the real trading position of a company is found, not in its balance sheet as such, but in its profit and loss account. Until the Companies Act of 1929 was placed upon the Statute Book, there was no legal insistence upon this account being included with a balance sheet for the information of shareholders. In the Act of 1929 it is laid down that directors shall lay before the company at its general meeting a profit and loss account or an income and expenditure account, and that one of these shall also be included in the balance sheet. Even so, the Act does not dictate the form which the profit and loss account shall take, beyond requiring that the total amount paid in remuneration to directors shall be shown, and even from this item the salaries paid to managing directors are excluded.

In the case against Lord Kysant and Mr. Morland, as regards the balance sheet charges, it was upon the profit and loss account that the interest turned. The R.M.S.P. Company, in common with many other companies, had made it a practice to issue a profit and loss account which showed the trading profits, dividends on shares in

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allied and other companies, adjustment of taxation reserves, less depreciation, and other items, in one entry. Nobody not in the fullest confidence of the company could distinguish which of the several items included had contributed to the sum of the total or in what proportion.

Under even the latest Act, that of 1929, which did not govern the years under discussion during the Kysant case, there is a specific limitation of the responsibility of the auditor to the balance sheet. In legal theory the auditor's duty is to certify that the balance sheet is so drawn as to exhibit a true and proper view of the company's affairs at a given date. If the amount carried to the balance sheet from the profit and loss account is correctly stated, and if it is a figure not fraudulently reached, an auditor would be justified in giving a clean certificate. In other words, it is not the legal duty of the auditor to insist upon a profit and loss account being framed which will show in detail the individual contributions to profit or loss.

But, it can be argued, it is at least the auditor's moral duty so to insist. How otherwise can he fulfil his obligation to the shareholders, whose representative and protector he is by virtue of his office? The state of the law even now is thus that an auditor is saddled with a grave moral responsibility for the fulfilment of which he has no legal power beyond his power of report.

The acquittal of Lord Kysant and Mr. Morland on the balance sheet charges probably did more to arouse the public and professional conscience in this matter than their conviction could have done. Had they been found guilty of an offence against the law, it might well have been thought by the public and the accountancy profession that legal provision was in existence which safeguarded the shareholder and the public, provided a sufficiently sharp eye were kept for those transgressing the admittedly wide boundaries of contemporary statute law. Their acquittal drove home the fact that the law itself was at fault, and that even the most recent Act, designed to amend many weaknesses in the law, itself omitted two vital provisions—that the profit and loss account presented to shareholders should follow a prescribed form which would make it impossible for “omnibus” items to mislead, negatively or positively, the reader, and that the auditor's legal responsibility should be extended to a certification of that account.

From the balance sheet charges arose also the discussion of the question of the legitimacy and the legitimate usage of hidden reserves, but this consideration may well be deferred here until after we have glanced at the significance of the prospectus charge, upon which Lord Kysant was convicted.

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The prospectus which invited the public to subscribe £2,000,000 of debenture stock naturally, as prospectuses tend to do, placed the rosier aspect of affairs before the potential suppliers of capital. He who issues a prospectus is endeavouring to sell an interest in his concern to the public, and no salesman, traditionally, cries "stinking fish," and no salesman can be blamed for putting the most favourable gloss upon the facts concerning that which he attempts to sell. So much is the tendency of prospectuses to exaggerate the excellence of the offer recognised that a passage of warning written by Mr Hartley Withers has become famous. It has been often quoted and is quoted again here.

All prospectuses (wrote Mr Withers in his "Stocks and Shares") should be scanned in a spirit of jaundiced criticism, and with the most pessimistic readiness to believe that they are speciously alluring traps laid by some designing financier to relieve the reader of some of his money. No allowance should be made, and the benefit of the doubt should never be given to the prospectus. In fact, a large number of them are quite reasonable propositions put forward by quite honest men, but when they are of this kind they will, or ought to, stand the most sceptical scrutiny, and when they are not it is a service to the community at large to put them as quickly as possible in the waste-paper basket. When they arrive by post or thrust themselves on your attention in the columns of your newspaper, your first instinctive thought should be that here is somebody wanting your money, and that he may be a descendant of Dick Turpin throwing back to his distinguished ancestor, and practising brigandage in a more modern and much less attractive form.

In this historic piece of advice to investors Mr. Withers, it will be seen, makes two points. One is the direct assertion that a reputable and legitimate invitation to subscribe capital will, or should, stand a sceptical scrutiny, and the other is the statement by inference that even within the law there is scope for unscrupulous men to mislead the public by the wording of the prospectus.

The essence of the charge against Lord Kylsant was that the statement which I have quoted on page xiv as to the average available balances was intended to convince the reader that the company for the past ten years had made a trading profit every year of about £500,000, whereas during the seven years preceding the issue of the prospectus the company had every year made a heavy trading loss.

A reference to the prospectus, reprinted on page 273, will also show that preceding a statement of the dividends paid on the ordinary stocks during the past seventeen years was a paragraph which read—

After providing for all taxation, depreciation of the fleet, &c., adding to the reserves, and payment of dividends on the preference stocks, the dividends on the ordinary stock during the last seventeen years have been . . .

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The Crown contended that any one reading the document, even with great care, would assume that the dividends had been paid, at the rate stated, out of the trading profits of the company, and that the words "adding to the reserves" would, at any rate, mean that the company had made its profits although it had been adding to reserves.

Although it was true that at the end of 1927 the reserves were higher than at the end of 1911, counsel for the Crown contended that the words "adding to the reserves" had somehow to be reconciled with the fact that the reserves, in order to provide the dividends, had been raided at the rate of £500,000 a year for the years immediately before the prospectus was issued. The words, it was submitted, amounted to a definite assurance that the earning capacity of the company produced those balances.

To quote Mr. Pritt's simile to the Guildhall Court, the trouble was that "the old-gentleman business was not making money, and the old gentleman was living on the savings of his prudent middle age."

The business of the Crown was to prove that Lord Kylsant was responsible for the wording of the prospectus; that he was aware that the company was losing money year by year and was living on its savings; and that the prospectus was designed to mislead the investors as to this position. This proof the Crown established, but in so doing provoked the interesting point as to whether a document could be false in a material particular when it contained no statement that was not perfectly true.

Before returning to the financial interest of the case as it turned upon the legitimacy and legitimate use of hidden reserves, we must examine this legal point with some attention.

The arguments of counsel, it will be seen, turned largely upon the interpretation to be placed upon section 84 of the Larceny Act of 1861, upon which the indictment had been framed. Old as the Act was on the Statute Book, this was the first case of its kind to be brought to hearing under that section. The actual grounds of appeal against the verdict of the lower Court were—

(1) That there was no evidence that the appellant made or published, or concurred in making or publishing, a written statement which was false in any material particular.

(2) That there was no evidence that he made or published the prospectus knowing it to be false in any material particular.

(3) That there was no evidence that he made or published a prospectus which he knew to be false in a material particular with intent

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to induce persons to entrust or advance property to the Royal Mail Steam Packet Company; and

(4) That the Judge at the trial had misdirected the jury.

Making the point before the Court of Appeal that the question was whether the document was one which contained a statement known to be false, counsel for Lord Kysant (Sir John Simon) said—

The real test, I apprehend, is : Is that which is said to have been omitted deliberately omitted and of such a character that if it were added the words that are used are shown to be false? I suggest that if that is the true test, after the verdict of the jury on the first and second counts (i.e., the balance sheet charges on which Lord Kysant was acquitted) there is no justification for the verdict on the third count. The question is not whether there is not some material which some one might want to consider. It is whether the thing which has been omitted, if you imagine it to be added, makes that which is affirmatively stated a lie.

In developing his argument, Sir John declared that it was a wrong construction of section 84 of the Larceny Act of 1861 to hold that under it there must be communicated to the shareholders or subscribers anything which it might be material for them to know, and that the criminality of a prospectus was not to be tested by seeing if anything was omitted which somebody might like to have been told.

In reply the Attorney-General reminded the Court of Appeal that in his speeches to the jury he had made it plain, and Mr. Justice Wright had also made it plain, that what was meant by the use of the word "false" was that by stating some things and omitting others a false impression was created. He submitted that what was said, in the absence of what was omitted, created a false impression as to the true nature of the company, and if that were so, the jury was perfectly entitled to come to the conclusion that the prospectus was a false document.

Mr. Justice Avory, who delivered judgment, swept aside the third ground of appeal, with the remark that it was immaterial, since it was admitted that if the prospectus was published and was false and known to be false there could be no doubt that it was published with intent to induce persons to entrust or to advance property to the company. As to the question of what was the test of a false document, he had little difficulty in citing authorities who supported the plea of the Attorney-General and the judgment of Mr. Justice Wright. In 1900 Lord Macnaghten had said : " It is a trite observation that every document, as against its author, must be read in the sense it was intended to convey, and everybody knows that sometimes half the

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truth is no better than a downright falsehood." Earlier, in 1896, Lord Halsbury had said in the House of Lords: "If by a number of statements you intentionally give a false impression and induce a person to act upon it, it is not the less false, though, if one takes each statement by itself, there may be difficulty in showing that any specific statement is untrue."

Mr. Justice Wright, in summing up to the jury, had said that to confine section 84 to exclude from "falsity in any material particular" that "type of fraud which may be found in a document, not fraudulent in the sense of what it states, but in the sense of what it conceals or omits" was "to narrow unduly the words 'in any material particular.'" In the Court of Appeal, supporting this interpretation, Mr. Justice Avory said: "The falsity in this case consists in putting before intending investors, as material upon which they can exercise a judgment as to the existing position of the company, figures which apparently disclose the existing position, but in fact conceal it."

On the further question as to whether there was evidence upon which the jury could properly find that the appellant knew the document to be false, Mr. Justice Avory said that if there was evidence that it was false in the particulars already indicated, there was ample evidence upon which the jury could find that the appellant knew of its falsity, knowing as he did the means by which the dividends had been paid.

During the hearing of the appeal, Sir John Simon, for Lord Kylsant, made one admission in his closing speech that both emphasises one of the significances of the Kylsant case and indicates its weakness as the strong moral lesson it might have been. Sir John had to confess that he, himself, did not regard the prospectus as a highly satisfactory one. He pointed out that a law had since come into operation (the Companies Act of 1929) which requires that prospectuses shall contain positive statements as to past profits, but that the new law did not affect the case they were considering. While that most painful inquiry had called specific attention to the desirability of giving more information—and nothing he had argued was intended to suggest the contrary—Sir John submitted that on the law as it stood at the time, although his client might have been too sanguine, he was never guilty of a fraudulent or false statement.

This would seem to suggest that Lord Kylsant's counsel was pleading, not a moral innocence, but a legal innocence, possible only as a plea because of the tardiness with which the law had been brought into conformity with the public conscience in such matters. Sir John, it



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must be remembered, was pleading before the Court of Criminal Appeal, where he was not entitled to urge moral innocence, as he had done before the lower Court, but that the defence should make such an admission and such a plea justifies fully the conviction that to the importance and significance of this case in 1932 the conviction or acquittal of the accused was incidental only—what mattered was the public revelation that the minimum demands of the law fell so far short of a common conception of honesty and fair dealing.

Quite apart from the changes made in the law by the Companies Act of 1929, the Kysant case definitely made it plain to the legal and financial layman that even under earlier Acts no applicant for the money of the public could with impunity deceive those whose confidence he solicited by merely stating a collection of facts each of which was incontestable but all of which, either by their method of presentation or by omissions of other facts, conveyed a false impression.

Such was the general lesson of the case. The main technical question which it raised—apart from that of an auditor's responsibility for certifying the profit and loss account—was as to the legitimacy and legitimate use of secret reserves. By paying dividends from such reserves without revealing their origin or amount the Royal Mail Steam Packet Company had deceived the public as to the true state of its fortunes at the moment when the disputed balance sheets were issued and at the time when it appealed for more debenture capital. Not the least cogent part of the summing up of Mr. Justice Wright will be found to turn upon a distinction which must be kept clear in the mind if the technical lesson of the case is not to be misconstrued. The distinction which the learned judge emphasised is elementary—it is between establishing and maintaining secret reserves and drawing upon them for dividend purposes without disclosing the fact to the shareholders.

Keeping in mind the first objection to secret reserves, which is that unless a shareholder knows what resources his company possesses he cannot assess the value of his shares or judge the wisdom of dispossessing himself of them at a given time, the value of such a prudent resource against times of financial trouble must be weighed against the inherent dangers which were suddenly exposed to many minds by the Kysant trial. Said Mr. Justice Wright to the jury—

A great deal has been said about the keeping of secret reserves, and how far that is or is not permissible under the Companies Act or under the special charter of the Royal Mail Steam Packet Company, because, as you will remember, the questions which arise here fall to be decided, so far as that aspect of the matter is for your decision or your consideration at all, under the special charter of that company. We have heard a great deal about the keeping of secret reserves, and

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we have heard a great deal about the commercial troubles which may flow from that practice. We have heard a great deal about what is often done in practice, and it may be reasonably and properly done, but the question may arise some day, and possibly will arise, in some appropriate proceeding in order to find out and elucidate these very special matters. It was said by a very learned Judge on one occasion by way of observation and not by judgment that a company, that is to say the shareholders, could not complain if the position of the finances of the company were better than the accounts disclosed. That has been quoted from time to time as a justification for this method of keeping reserves secret. But there may be very great evils if those who have the control and management of the company, and who control and manage companies for the benefit of the shareholders who entrust their moneys to companies, have very large portions of the company's assets left in the secret disposition of the managing authority. It may work very well in many cases: no doubt it does. It is a practice which is being followed, no doubt, by many concerns of the highest standing. On the other hand, it may be the subject of almost intolerable abuse. Such a system may be used to cover up negligences, irregularities, and almost breaches of faith. It is said to be a matter of domestic concern between the company and the shareholders, but if shareholders do not know and cannot know what the position is, how can they form any view about it at all.

In presenting a balance sheet, those in control of large and competitive companies very frequently find themselves on the horns of a dilemma. Their duty to their shareholders—who are, after all, the proprietors of the business—may dictate frankness to the uttermost possible degree in order that those shareholders may “form a view,” but their duty to the enterprise may dictate a certain prudence in order that information, valuable and stimulating to the firm's competitors, may not be revealed to the ultimate detriment of the concern. It becomes in some minds a fine point whether this aspect of directorial duty does not equally affect discretion in preparing a prospectus. It is no excursion into sophistry which leads many a board of directors to withhold information from the shareholders on the justification that such a withholding is really for the shareholders' own good.

The law, however, is in no two minds about which aspect of directorial duty should outweigh the other.

It must be remembered at every stage of the Kysant trial that the charges were made in reference to actions committed before the passing of the Companies Act of 1929. By that Act all prospectuses are compelled to contain a report by the auditors of the company as to the profits of the company for each of the three financial years immediately before the issue of the prospectus. Had the Royal Mail prospectus been issued under that compulsion, the charge, against a conviction on which Lord Kysant appealed, would not have arisen. That prospectus, as

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will be seen, contained no report of the auditors and the profits of the individual years were not specified.

The Kysant case differs in kind from the Hatry and Kreuger cases. Hatry and Kreuger were guilty of deliberate fraud made possible by recourse to forgery. Against such fraud it is difficult to devise preventive measures. There was no such positive fraud in connection with the Royal Mail prospectus, and none alleged in connection with the balance sheet charges. The deceit which was alleged was negative, and consisted in a lack of frankness. As I have suggested in the preceding paragraph, the Companies Act of 1929 does furnish a safeguard against such prospectuses misleading the investor in the future, but the possibility of issuing a misleading balance sheet which shall still be within the law is still given to unscrupulous directorates aided by careless auditors. This aspect of the position, as the Kysant trial emphasised it, continues to engage the thought of the leaders in the profession of accountancy, and has driven Mr. Henry Morgan, the then president of the Society of Incorporated Accountants and Auditors, to a virtual crusade of reform.

The vital weakness, as Mr. Morgan and a special committee of his society see it, is the lack of compulsory information contained in published profit and loss accounts. The Act of 1929 contains comprehensive provisions as to the form and contents of the balance sheet and its certification by an auditor: it has no such provisions as to the profit and loss account. Before that Act there was no legal compulsion upon directors even to publish a profit and loss account. Section 123 of the Act, first sub-section, provides that directors of every company shall lay before the company in general meeting a profit and loss account or an income and expenditure account, but it says nothing of the form which these accounts shall take, or the amount of minimum information they shall contain. (It is true that the Act makes it obligatory to show the total amount paid in remuneration to directors, but that obligation is largely negated by the omission from the compulsion of the amount paid to salaried directors.) Reticence about the profit and loss account may result in the shareholders or potential shareholders drawing the most erroneous conclusions as to the standing of the company.

In the Kysant trial the case against the auditor turned almost wholly on the profit and loss account. As we have seen, the Royal Mail Company had been in the habit of issuing such an account showing the trading profits, dividends on shares in allied and other companies, adjustment of taxation, less depreciation, &c., in one combined item.

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“ Profits ” or “ revenue ” was not shown as a distinct and separate heading. This procedure was by no means singular. Many companies used it. It is legitimate even under the Act of 1929. But a profit and loss account is misnamed which does not show profit and loss for the period of the accounts presented, which, that is to say, adds to such profits, or subtracts from such loss, amounts brought in from reserve or expenditure made in some other period.

The position of the auditor is peculiar. Under the terms of the Companies Acts his certificate is definitely restricted to the balance sheet. No matter how uneasy he may feel as to the form of the profit and loss account, he cannot communicate his ill ease to the shareholders, whose interests he guards. In such a position, what is he to do? Mr. Henry Morgan has said—

Some leading members of the profession believe that his only course is to refuse to certify the balance sheet, although no exception can be taken to the balance sheet itself. This would put the auditor in a position of great difficulty. He would be in conflict with the directors, whose intentions might be genuine, and the drastic action which he considered necessary might have serious consequences to the company concerned. It is to the credit of the accountancy profession that cases are rare in which auditors have sought to avoid their obligations, but it is not desirable or equitable that the question of the auditor's responsibility for the profit and loss account should remain in an indefinite state, or that the auditor's powers should be of a merely negative character

Mr. Morgan's own solution is that there should be provisions in the Companies Act defining the general form and contents of the profit and loss account, just as there are provisions affecting the balance sheet, and the auditor's responsibility for the profit and loss account should be placed beyond all question. The auditor's certificate should, that is to say, contain some phrase such as “ the profit and loss account is a true and correct statement showing the profit earned (or the loss incurred) during the period covered by that account.” There is, however, another viewpoint, from which the rigid definition by legislation of the general form and contents of the profit and loss account threatens to do more harm than good. I have said that the auditor is, in theory, the watch-dog of the shareholders. He is their servant. But so, too, are the directors. The service which the directorate of a company gives to the shareholders is not merely that of dividend providing in any particular year. The moral charge upon a board is to keep the company prosperous, and at any point in the life of a trading entity there may arise circumstances in which a disclosure to the proprietors of the exact trading profit for an arbitrary balance-sheet year may give to trade competitors information which might lead to such intensified

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and unfair competition that the company would gravely suffer. Men of business are familiar with many examples of this in recent commercial history. To take an hypothetical case—founded, as the old novelists used to say, on fact—if an English enterprise were confronted by a strong attack by some American competitor conducted in such a way that the endeavour to undermine the home market involved the American firm in temporary losses, the fact that the English firm had also suffered losses would be an incentive to the competitor to continue and even to intensify his competition. The application of inner reserves by the English company to provide dividends, and an appearance of continuing prosperity, for a year or two, would technically be misleading to the shareholders, but it would also be misleading to the competitor, and might very well persuade him that a war of trading attrition was a hopeless project. In such circumstances freedom to refrain from rigidly showing true profit and loss for the year would permit the company to survive where a lack of such freedom might drive it to ruin, with all the consequent loss to the shareholders and unemployment and hardship to the employees.

Again, the cases of unscrupulous or stupid directorates abusing the present lack of legal definition are few: the cases of professional auditors prepared to condone such abuse, even fewer. Hard cases traditionally make bad law. If it were possible to define a minimum requirement for the contents of a profit and loss account, if it were possible to ignore the fact that no absolute rule can be framed to apply to every case, and if the Legislature were able and prepared to extend the responsibility of the auditor from the balance sheet to the profit and loss account as such, it would still be doubtful if the gain would outbalance the harm of such a change. As Lord Plender implied, in his address to the Chartered Accountants Students' Society of London at the annual meeting of 1932, a rigid law might create grave evils, whereas the widening sense of responsibility in the accounting profession may cure those evils which have been shown to exist. In Lord Plender's own words—

If the members of our profession were to look on this matter purely from the standpoint of their own personal interests, there would be much to be said in favour of legislation which might relieve an auditor of any doubts as to what was his duty under certain sets of circumstances. He might in such a case be compelled by law to take a certain line of action which he might believe to be inimical to the best interests of the shareholders in the company concerned. Discretionary power would be taken from him and his responsibilities would, therefore, be lessened. But I suggest to you that we must take a wider view than this. The true interests of our clients must come first, and if this can only be achieved by our assuming greater responsibilities we must be

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prepared to shoulder those responsibilities. (Reported in *The Accountant*, 14th May, 1932.)

But it must be emphasised that the shouldering of responsibilities by the auditor is not enough: there must be a readiness in the company directors to accept similar views of what is right, for, Lord Plender continued—

What causes me no little surprise is that directors of public companies who are vitally interested in the subject refrain from expressing their views. Many of them are giving fuller information in accounts, but there are others who have set themselves against more disclosure than a minimum *in spite of advice the auditor may give*. Lack of information in many cases in regard to subsidiary companies' assets, liabilities, and trading results is a matter which seems to me to call for action on the part of shareholders, and if legislation in regard to company accounts is contemplated this particular matter should, in my opinion, receive consideration.

On another occasion, addressing the Insurance Institute of London in February, 1932, Lord Plender went further—

I see (he said) grave difficulties in attempting to stereotype forms of balance sheets and profit and loss accounts, and I am not prepared to say what is the minimum information which every profit and loss account should disclose. There is such a variety of cases, each differing from another in certain respects; there are so many thousands of companies not identical in objects or in the class of business conducted; there are so many problems of a special and not general character affecting one or a group of companies which do not touch others—that uniformity in presentation of accounts or in the amount of information to be given cannot easily be legislated for. . . . I think that directors may well, in many cases, give, without danger to a company's interests, more information to the shareholders than is the case at present, but the degree and extent of such information cannot be universally applied; it must be influenced by the character of the business, its methods of trading, and other considerations that have a special or peculiar bearing on the company itself. In this connection, whilst I feel, for the reasons given, that a stereotyped form of profit and loss account is impracticable, I think that in the preparation of all profit and loss accounts certain general principles should be followed in order to ensure as far as possible that the net results fairly attributable to the year's operations upon a basis comparable year by year should be shown and that extraneous and abnormal items should be stated separately.

The Royal Mail case, it is clear from the above quotations of opinion, launched a controversy upon whether amendment of the law with regard to the preparation of profit and loss accounts is practicable or desirable, but it revealed unanimity of view in the controversialists that in many cases, law or no law, prevailing practice demands amendment.

The Kysant case, it may thus be said, in conclusion, has three lessons for those who read its significances aright, each of which is a salutary reminder to directors, auditors, and shareholders of legal and

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financial actualities. The first is that the law holds, with perhaps unusual common sense, that a statement is capable of misleading the reader though it contain no specific inexactitude of fact. The second is that a balance sheet which is not accompanied by a detailed and frank profit and loss account may be misleading as to the existing position of the company, and is unlikely to be a sound guide to the current value of its shares. The third is that the auditors, upon whom the shareholders and public rely for protection, are handicapped partly because their exact responsibility to the profit and loss account is undefined—counsel's opinion on this point circulated to members of the Institute of Chartered Accountants went no further than to say: "In our opinion, having regard to the fact that the balance sheet contains as one of its items the balance brought in from the profit and loss account, they cannot dissociate themselves from all responsibility for the correctness of that account, and there may be cases in which it would be incumbent upon them to draw the attention of the shareholders to any feature of that account which in their view involved anything of an improper or misleading character"—and partly because their influence upon the directorate in determining what use shall be made of, and what frankness exercised upon, such items as secret reserves depends not upon a defined status and power of intervention, but upon the personal relationship of two professional persons each to the other. The strain upon a timid auditor or an auditor chary of risking a valued, and perhaps vital, connection, to refrain from protest or the giving of advice is thus so great that it is unjust to the auditor and dangerous for the people whose interests he is attempting to protect.

What amendments of company law may follow the general and still-growing realisation of these lessons is uncertain. That special legislation will be introduced is unlikely, but it is quite certain that future Acts affecting company law will be framed very largely in the light of those lessons. It is this conviction which justifies the publication of this volume, where a record of the case is made available to those who would otherwise have to refresh their memories from newspaper files or the relatively inaccessible records in official keeping.

## Crashes and Crises of the Last Decade,

1920-1932.

- May, 1922, Great Britain.** Horatio Bottomley: convicted in connection with conversion of public subscriptions to various clubs, formed for the purpose of purchasing War Savings Certificates, National War Bonds, Victory Bonds, &c. Sentenced to seven years' imprisonment, appeal dismissed.
- June, 1922, Great Britain.** Gerrard Lee Bevan: Frauds in connection with the failure of the City Equitable Fire Insurance Company, followed by the liquidation of its subsidiary companies and the bankruptcy of Bevan's firm, Ellis & Co. Arrested in Austria in July. Brought to London and sentenced to seven years' penal servitude on 6th December, 1922.
- June, 1925, Germany.** Firm, Hugo Stinnes: split at the end of May between the two sons of Hugo Stinnes, Dr. Edmund Stinnes, and Hugo Stinnes. The crisis in the house of Stinnes was due to "bad financial dispositions and faulty organisation of the proprietors." Banking difficulties later and firm was helped by the leading German banks. Reconstruction was carried out late in the year and a new 25,000,000 mark company — Stinnes Coal Trade Co. — was floated.
- July, 1928, America.** Captain Lowenstein. Mysterious disappearance of Captain Lowenstein from a cross-channel aeroplane, followed by heavy bear operations in International Holding and Investments Co. and Hydro Electric Securities Corporation. Panic averted and recovery later.
- Jan., 1929, Great Britain.** Ner-Sag, Ltd. Following the appointment of a new chairman, the retiring chairman, O. A. Brandreth, failed to answer satisfactorily certain important questions asked by the reconstituted board of directors re the history of Ner-Sag, Ltd.; heavy selling on the Stock Exchange followed and the disappearance of Mr. and Mrs. Brandreth led to inquiries. Mr. Brandreth was found guilty of publishing a false balance sheet and of making false entries in an invoice book, and was sentenced in May, 1929, to four years' penal servitude.



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- August, 1929, Germany.** Frankfurter Allgemeine Versicherungs A.G. Failure of large German insurance concern owing to "heavy commitments in the shape of guarantees for consumption financing, in particular the sales of motor cars under the instalment system." Many speculative insurance deals. Reconstruction was later effected, but the chiefs were arrested in September.
- Sept., 1929, Great Britain.** Clarence Hatry. Collapse of the market in the shares of the Hatry Group, followed by the arrest of Clarence Hatry and his associates on 19th September. Heavy bear operations on London and New York exchanges. Hatry sentenced to fourteen years' imprisonment for false pretences and issuing fraudulent share certificates.
- Jan., 1930, Great Britain.** Blue Bird Oil Companies. Francis Lang arrested for certain irregularities in connection with the accounts of the Blue Bird Oil group. He was sentenced in November, 1930, to seven years' penal servitude for fraudulent conversion of £317,000 and with publishing a false statutory report.
- Nov., 1930, France.** Banque Adam suspends payments, following the collapse of the market in the shares of the Oustric group. The Coubissier authorities ordered quotations of five of the leading issues of the Oustric group to be summarily suspended. The Oustric Bank suspended payments and was wound up, a public inquiry being instituted into its affairs.
- Nov., 1930, Great Britain.** Royal Mail Group difficulties; Mr. Runciman appointed deputy-chairman of thirteen Royal Mail subsidiaries.
- Dec., 1930, America.** Bank of the United States closed its doors and a run on its associate banks was prevented by the action of the Federal Reserve Bank.
- May, 1931, Austria.** Credit Anstalt suspends payments. Panic in Austria and Central Europe. Mr. H. Hoover proposes one year's War Debts moratorium. Ratification of the proposal in August. Inter allied debts postponed.
- June, 1931, Great Britain.** Royal Mail Affair; Lord Kylsant and Mr. Morland committed for trial for issuing misleading accounts over a period of years. Lord Kylsant also charged with regard to a prospectus. Lord Kylsant sentenced to twelve month's imprisonment on prospectus charge only, and Mr. Morland acquitted. Kylsant appeal dismissed. Reconstruction scheme later adopted.

# Crashes and Crises of the Last Decade.

- July, 1931, Germany.** Danatbank suspends payments. German Bank Holiday proclaimed. "Standstill" agreement concluded in August.
- Dec., 1931, Sweden.** Kreuger & Toll anxiety; bear activity on the world's stock exchanges.
- March, 1932, Sweden.** Kreuger & Toll. Ivar Kreuger commits suicide in Paris. Investigations by international committee revealing gross frauds by M. Kreuger. Estimated by the Swedish committee of experts that at the time of his death, M. Kreuger's debts amounted to nearly £50,000,000. Shareholders and other unsecured creditors expected to get little or nothing.
- April, 1932, Great Britain.** Scottish Amalgamated Silks. The seven promoters of Scottish Amalgamated Silks were charged with fraud and misappropriation, and with issuing a false prospectus. Alexander Young and George M. Todd were found guilty of defrauding the public of £439,348 by means of a false prospectus and of misappropriating £362,733 by fraudulent share allotments. They were sentenced to three years' penal servitude and six months' imprisonment respectively. At the appeal, the sentences were reduced; for Young to eighteen months' and for Todd to three months' imprisonment. The other promoters were dismissed.



# THE TRIAL

WITHIN THE  
CENTRAL CRIMINAL COURT,

Old Bailey, London,

MONDAY, 20TH JULY, 1931.

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*Judge—*

MR. JUSTICE WRIGHT.

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*Counsel for the Prosecution—*

The ATTORNEY-GENERAL (Sir William Jowitt, K.C., M.P.).

Mr. D. N. PRITT, K.C.

Mr. EUSTACE FULTON.

(Instructed by the Director of Public Prosecutions).

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*Counsel for Lord Kylsant—*

Sir JOHN SIMON, K.C., M.P.

Mr. J. E. SINGLETON, K.C.

Mr. WILFRED LEWIS.

(Instructed by Messrs. Holmes, Son & Pott).

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*Counsel for Mr. Morland—*

Sir PATRICK HASTINGS, K.C.

Mr. STUART BEVAN, K.C., M.P.

Mr. C. J. CONWAY, K.C.

Mr. F. J. TUCKER,

(Instructed by Messrs. Slaughter & May).



## First Day—Monday, 20th July, 1931.

[At the outset Sir John Simon intimated that he desired to make a submission before the defendants were asked to plead. Referring to the indictment, he said that it contained three counts, and he wanted the judge to consider whether or not, in fairness to the defendants, greater particularity should not be shown in making the allegations which the indictment contained]

Mr. Justice Wright said that the defendants would plead, the case would be opened, and at the end of the opening the question of whether there should be further particulars or not would then be discussed.

After the indictment had been read over and the accused had pleaded not guilty, Sir Patrick Hastings raised the question of the severance of the counts. He said that under the new Act, where the Court was of opinion that a person might be prejudiced or embarrassed by reason of being tried for more than one offence, the Court might order a separate trial of any count or counts.

His lordship said that in his judgment the trial of the indictment should proceed as a whole.]

**THE CLERK OF THE COURT**—Owen Cosby Philipps, Baron Kysant, and Harold John Morland: you are charged in an indictment containing three counts. The first count charges you, Lord Kysant, that you on the 11th May, 1927, being a director of the Royal Mail Steam Packet Company, did make, circulate, or publish, or concur in making, circulating, or publishing, a certain annual report of the company for the year 1926, which you knew to be false in a material particular, and that the said annual report concealed from the shareholders the true position of the company, with intent to deceive the shareholders; and you, Harold John Morland, are charged with aiding and abetting Lord Kysant to commit that offence. In the second count, you, Lord Kysant, are charged that on the 9th May, 1928, being a director as aforesaid, published an annual report for the year 1927, which you knew to be false in a material particular, with intent to deceive the shareholders; and you, Harold John Morland, are charged with aiding and abetting Lord Kysant to commit that offence. The last count charges you, Lord Kysant, that you, on the 29th June, 1928, being a director as aforesaid, did publish a prospectus inviting the public to subscribe to the issue of debenture stock in the Royal Mail Steam Packet Company which you knew to be false in a material particular, in that it concealed the true position of the company, with intent to induce persons to entrust or advance property to the company. Lord Kysant, are you guilty or not guilty?

**LORD KYLSANT**—Not guilty.

**THE CLERK OF THE COURT**—Harold John Morland, are you guilty or not guilty?

**MR. MORLAND**—Not guilty.

# The Royal Mail Case.

## Opening Speech for the Prosecution.

The ATTORNEY-GENERAL—May it please your lordship, members of the jury, you have just heard the charge read with which the two defendants are accused. It is an offence under a section of one of our Acts of Parliament for any person who is a director of a company to publish a written statement or account which he knows to be false in any material particular, with intent to deceive shareholders. It must be false, he must know it to be false, and there must be an intent to deceive shareholders. Lord Kylsant is charged that he did on 11th May, 1927, and 9th May, 1928, publish accounts in respect of the years 1926 and 1927 of the Royal Mail Steam Packet Company of which he was a director. Mr. Morland, who acted as auditor for that company during those years, is charged with aiding and abetting Lord Kylsant in doing so. By a different set of words in the same Act it is further made an offence to publish a written statement or account which you know to be false, with intent to induce people to lend or entrust money or property to the company. Lord Kylsant is charged with a breach of those words by reason of the issue of a prospectus which he issued on 29th January, 1928. You must remember throughout Mr. Morland had nothing whatever to do with that; no charge is made against Mr. Morland in respect of that at all, and therefore in opening this case at this stage I propose to leave that out altogether and address my observations to you just as though the only two charges against him were the charges in respect of the accounts which deal with the years 1926 and 1927, with regard to which both defendants are indicted, Mr. Morland with having aided and abetted Lord Kylsant.

Let me explain to you in a word what my position as Attorney-General, or what in fact the position of any prosecuting counsel in this case or in any criminal case, is. I am not here to endeavour to secure a conviction and to try to ride round and escape from the rules of fairness or anything of that sort. My task is merely to put before you as best I can the plain unvarnished facts, without rhetoric and without emotion, in order that you may be assisted to come to your decision as to whether these defendants are or are not guilty of the offences with which they are charged. Every man in this country, rich or poor, peer or peasant, is bound by the same law, and must observe the same law; and whilst on the one hand no favour must be shown to a man because of his wealth or position, so on the other hand no man, merely because of his prominent public position, must be made a target for unfair or unworthy attacks.

Lord Kylsant, as I have told you, was a director of the Royal Mail Steam Packet Company, and I have no doubt that directors of companies not infrequently find themselves in difficulty with regard to the management of their companies and the publication of their accounts. One can understand that a director of a company may be reluctant, if things are going badly, to expose the nakedness of the land and to

# Opening Speech for the Prosecution.

The Attorney-General

advertise to the world the fact that his company is in difficulties. One can well understand anybody being reluctant to frighten timid shareholders or to encourage competitors. Whatever the difficulties may be, directors of companies, like you or I, or any of us, are bound by the law. We are not entitled to publish a document which we know to be false, with intent to deceive. In the same way I have no doubt that an auditor of a company not infrequently finds himself in a position of some difficulty. An auditor, as you know, is not a mere servant of the directors, bound to do what the directors want him to do. He is not merely an official in some, I was going to say, mystic or mysterious science called accountancy, and he is certainly not performing a mere ministerial act or a mere piece of mumbo-jumbo when he gives a certificate which affects the company's accounts. In one case not long ago in the Courts he was well described as a watch-dog to see that the shareholders and their interests are adequately safeguarded and observed. When an auditor signs an account as he does. "In my opinion this balance sheet is properly drawn up so as to exhibit a true and correct view of the company's affairs as shown by its books," then he is stating something upon which the ordinary investor is entitled to rely, and he is stating something which he must know will be a matter which the ordinary investor will take into consideration. So you have to find in this case that a document was false in a material particular, that it was known to be false, and that there was an intent to deceive. The accused are entitled to say that facts must be brought home against them beyond reasonable doubt, and I, as representing the Crown, should be the first to say that, if you have any reasonable doubt, they are entitled to the benefit of it.

Let me give you this one observation with regard to the word "intent," intention to deceive. Let me ask you to have quite clear in your mind the distinction between "intention," which means that a man knows what he is doing and deliberately does it, and "motive," which is an absolutely different thing, a thing very difficult to find out and ascertain, a thing which does not matter in our Courts so long as the intention is there. Motive, of course, is sometimes used in these Courts as a factor to be considered in ascertaining whether a certain person has committed a certain crime. Motive is frequently a very material factor in enabling a judge to come to a fair conclusion as to what punishment, if any, should be inflicted. Whether the motive is the motive of personal enrichment, or the motive which springs from a false pride in being reluctant to let the true position of the company be known, or the motive even of protecting shareholders by putting forward that which is untrue, a desire to retain a distinguished personal position, or the desire to avoid having to take a course which would lead to unpleasantness and bickering—whatever the motive may be does not matter, so long as you find that there is an intention to deceive.

This case, like all cases in these Courts, must give one considerable anxiety, anxiety none the less, indeed the more, because the two men who are now being tried are men who bear honourable and distinguished



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## The Attorney-General

records both in public and private life Lord Kysant has had for many years a distinguished public career. He has risen to be chairman, and since 1907, I think, has been chairman of this Royal Mail Steam Packet Company, which, with its associated companies, owns or controls a very large amount of our shipping. Mr. Morland has been for many years a partner in one of the foremost accountancy firms in this city, the firm of Price, Waterhouse & Co., whose name must be familiar, I suppose, to everybody who reads the papers, and he, like Lord Kysant, has had a very distinguished career. It is right that I should say, and say quite emphatically, that prior to the allegations which we are now investigating, no suspicion at all, no possible doubt has been cast upon the integrity and the honesty of the two men whom you are now trying. That is a very relevant factor for you to take into consideration when you are considering whether there was or was not an intention to deceive. There is just this other side of the picture: great positions carry with them great responsibilities. Caesar's wife should be above suspicion, and it is an obvious fact that we must look to those who have achieved great positions in our public life in the life of this city to uphold untarnished its great records for fair and straight dealings. If you find in this case that these accounts were false, it is obviously a case I say to you, since you are not dealing with inexperienced men—you are dealing on the one hand with a very eminent accountant, and you are dealing on the other with a very eminent City man, with a full knowledge of the circumstances—if the accounts are false, I think you are bound to come to the conclusion that they were known to be false. And if you come to the conclusion that these accounts were known to be false, you must, in my submission, come to the conclusion that persons who put forward accounts which they know to be false intend to deceive somebody. Who could that somebody be but the shareholders? And you will, I think, be the more irresistibly drawn to that conclusion, if you come to this conclusion—if you come to the conclusion that perfectly prepared phrases were made use of which would allay any suspicion or uneasiness in the mind of the ordinary prudent investor, which would conceal from him the true position, yet phrases so carefully selected as to enable the defendants to say: "Well, the possible meaning of the words we used, the subtle meaning, the refined meaning, the dictionary meaning of the words cover what we did." If you think that they carefully constructed phrases preventing the ordinary man understanding what was being done, then the very fact that the phrase was constructed in the way I have indicated will, in my submission, force you to come to the conclusion that there was an intention to deceive.

The constitution of the Royal Mail Steam Packet Company goes back into almost distant history. It is a company with a great history behind it. It was what we call a chartered company. As you know, most companies nowadays are joint-stock companies, formed under the Companies Acts, but this company goes back before those Acts. In those days companies used to be formed by royal charters, and the

# Opening Speech for the Prosecution.

The Attorney-General

Royal Mail Steam Packet Company had its constitution comprised in a series of royal charters, the first of which dates from 1839 and the last of which comes down to 1920. There are one or two passages in the charters which I ought to read to you to enable you to follow the points I am going to make hereafter. In the first charter there is this reference to accounts, and as the later charters do not deal with this I will read it—

And we do further will and ordain that previously to every yearly general meeting an account shall be prepared by the court of directors of the debts and assets of the said corporation, with an account of the profits made in the year ending the 31st December preceding such general meeting for the time being as near as the same can be ascertained, and with all such information as may to the directors seem necessary to be given or may be required by any bye-laws of the said corporation, which accounts shall be signed by at least one of the auditors of the said corporation, and shall be laid before such meeting to be audited and settled as aforesaid

Then they go on to constitute the court of directors—

And for the better ordering and governing the affairs of the said corporation and for making and establishing a continuous succession of persons of the said corporation, we do by these presents for us, our heirs and successors, grant unto the said Royal Mail Steam Packet Company and their successors, and we do hereby order and appoint that there shall be from time to time constituted in manner hereinafter mentioned out of the members of the said corporation a chairman and deputy chairman of the said corporation, who shall also be directors, and such other number of directors not exceeding ten as the special court of directors shall from time to time determine, and two auditors of the said corporation which the chairman, deputy chairman, and other directors or any three of the several directors shall constitute and be called a court of directors.

That set up a court of directors, but the words I want you to carry in your minds are with regard to the accounts. There was to be an account every year to be laid at the general meeting, firstly, of the debts and assets of the said corporation and, secondly, an account of the profits made in the year. I do not think I need read anything else in that charter.

In the third charter there is a power to issue debentures—the ordinary powers—and I need not, I think, read it to you. But in the fourth charter there is a passage which perhaps I ought to read to you—

Auditor need not be shareholder. And we do further will, direct and ordain that so much of the original charter as requires an auditor of the company to be a holder of stock of the company is hereby rescinded, annulled, and revoked, and that, notwithstanding anything in the said original charter contained to the contrary, the following provisions as to auditors and the auditing of accounts of the company shall have effect in substance for all such provisions of the said original charter with reference thereto.

That is to say, it provides that the company at each annual general meeting is to appoint an auditor or auditors to hold office until the next annual general meeting, and then it makes all sorts of provisions in case that does not happen. Then it provides—

Every auditor of the company shall have a right of access at all times to the books and accounts and vouchers of the company, and shall be entitled to require

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## The Attorney-General

from the directors and officers of the company such information and explanation as may be necessary for the purpose of the duties of an auditor, and the auditor or auditors shall sign a certificate at the foot of the balance sheet stating whether or not all his or their requirements as auditor or auditors have been complied with, and shall make a report to the shareholders on the accounts examined by him or them, and on every balance sheet laid before the company in general meeting during his or their tenure of office in every report shall state whether in his or their opinion the balance sheet referred to in the report is properly drawn up so as to exhibit the true and correct view of the state of the company's balance sheet as shown by the books of the company, and a copy of every such report shall be sent to each proprietor and shall be read before the company in general meeting

Then I may pass on to a later charter, paragraph 16, which deals with the remuneration of the managing director. Lord Kysant was the managing director and gave the directors power to fix the terms of his remuneration, and I shall have to explain to you the terms of the remuneration presently. Then paragraph 20 provides for payment of debentures out of revenue. I must read this to you—

The directors may before recommending any dividend set aside out of the profits of the company such sums as they may from time to time think proper as reserve, insurance, or suspense funds. All sums so set aside shall at the discretion of the directors be applicable for meeting any losses, contingencies, or any depreciation in any of the company's assets, or for the gradual liquidation of any debt or liability of the company, or for repairing, renewing, or maintaining any property of the company, or for equalising dividends, or for distribution by way of dividend or bonus among the members of the company in accordance with their rights, or for any other purpose which the directors in their discretion may deem to be for the advantage of the company. Provided that any such parts of any reserve or other fund as shall from time to time in the opinion of the directors represent undivided profits properly available for dividend shall be distributed by way of dividend or bonus.

21. The directors may either invest any moneys representing any part of any reserve, insurance, or suspense fund in such manner as they may deem expedient, or they may employ all or any of such moneys in the business of the company without being bound to keep such moneys separate from the other assets of the company. The directors may divide any reserve, insurance, or suspense fund into such special funds as they may deem expedient. The income of any such funds may at the discretion of the directors be treated as profits of the company or be dealt with in such manner as the directors may think fit.

Now, those are some of the salient passages in the charters of the Royal Mail Steam Packet Company. I have read them to you at this stage, and I shall have to refer to some of them later and make some observations about them. Now, I want you to understand the financial position of the capital and the outstanding debentures of the Royal Mail Steam Packet Company, and I shall try to put this to you quite simply. At all material times there were a number of debenture-holders; those debenture-holders, of course, as you know very well, are not shareholders at all; they are simply people who have lent money to the company and are secured creditors. There were a number of debentures outstanding, the number being as follows.—1,400,000  $4\frac{1}{2}$  per cent. debentures and there were 3,100,000 5 per cent. debentures. The service of these debentures involved an annual charge of £218,000. That is the yearly debenture interest. You appreciate that, of course, has to be paid before anything at all, otherwise, of course, the debenture-holders would foreclose and come in and, if necessary, sell the company

# Opening Speech for the Prosecution.

The Attorney-General

up. Subsequently there were shares and groups of preference shares, some of them 5 per cent. preference shares. There was a lot of 900,000 5 per cent. preference shares, and there was a lot of 2,900,000  $6\frac{1}{2}$  per cent. preference shares. I am told I am wrong; they were stock. Now the 2,900,000  $6\frac{1}{2}$  per cent. preference stock was created in 1921. The service of the preference stock, assuming you are going to pay all the preference stock in full, involves a yearly charge, and this is the next figure I want you to remember, of £233,500. Pausing there for a moment, you will see, if you add those figures together, that before you can consider your ordinary shares at all you must first of all pay up on your debentures £218,000, and then you must pay up on your preference shares that £233,500, and those two added together come to £451,500. In addition to that there was at all material times a quantity of ordinary stock, £5,000,000. Of course the dividend on the ordinary stock, as you appreciate, is not a thing which is fixed with a limit either way, up or down, but, to give you an idea how it works, you will find that, if you pay a 5 per cent. dividend, that involves you in the payment of £250,000, and, of course, each £1 per cent. is £50,000 up or down. A 6 per cent. dividend would be £300,000, and a 4 per cent. dividend would be £200,000, and the ordinary 5 per cent. dividend would be £250,000, and as that was a dividend frequently paid, on the assumption that the ordinary stock were getting 5 per cent., you will therefore see that for the service of the debentures, preference capital, and ordinary stock we should require a little over £700,000, that is to say, £250,000 plus the £451,500. That is what the annual charge would be, assuming that the ordinary stock is going to get its 5 per cent.

The Royal Mail Steam Packet Company owned six companies, which are generally referred to as the 100 per cent. subsidiaries, that is to say, with regard to each of those companies the Royal Mail Steam Packet Company held all their shares. Therefore, you will appreciate that every one of these subsidiaries, as a matter of legal theory, is a separate entity, and the Royal Mail Steam Packet Company is the only shareholder. The first is the Royal Mail Meat Transport, Ltd., with an issued capital of, I think, £1,000,000. The next was H. & W. Nelson, Ltd., who were a company really carrying on a brokerage or commission business, and they acted as managers for the Nelson Steam Navigation Company, Ltd., who were shippers. Then there are two companies, Robert M'Andrew & Co., Ltd., and David M'iver & Sons, Ltd.; and perhaps the most important of them comes last, the Pacific Steam Navigation Company with an authorised and issued capital of £1,500,000. Then there were a large number of associated companies which have very complicated interlocked shares which I do not think come into the picture at all—Elder, Dempster & Co., the White Star Line, Lamport & Holt, and so on. I am not going to trouble you with them, but in order that you may get some idea of the magnitude of this fleet of the Royal Mail Steam Packet Company, including the Royal Mail Meat Transport, it comes in round figures to something like 400,000 gross registered tonnage, and if you include the associated companies, the

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**The Attorney-General**

100 per cent. subsidiaries, you will have a total gross tonnage of round about 2½ millions. They are all grouped companies very closely interlocked and concerned.

Lord Kylsant was chairman not only of the Royal Mail Steam Packet Company, but he was also chairman of each of the 100 per cent. subsidiaries at all material times. He was paid some quite modest sum by way of fees by the subsidiaries for being their chairman, but the relevance of the fact that he was chairman is the fact which differentiates him from Mr. Morland, who had nothing to do with these companies, in that Lord Kylsant would either know the history and affairs of his companies, or at any rate would have the means of knowing, whereas Mr. Morland's position is different there. Lord Kylsant's remuneration, so far as the Royal Mail Steam Packet Company is concerned, is a matter of importance. It was settled in 1907, and his remuneration was one-half per cent. commission on the gross takings of the company provided that company paid in any year a dividend of 5 per cent. on its ordinary shares. If it did not pay 5 per cent. on its ordinary shares, then he got £3000, but if it did pay 5 per cent. on its ordinary shares, then he became entitled under the agreement to one-half per cent. on gross takings, which, as a matter of fact, were calculated on the earnings of the Royal Mail Steam Packet Company, including the Meat Transport, after deducting a proportion of through rates, cost of forwarding, and rebates thrown away. The relevance of that is this here again is a factor which applies to Lord Kylsant and has no relation to Mr. Morland at all. As far as Lord Kylsant is concerned, he had a very direct personal pecuniary interest in having a dividend of 5 per cent. paid, because, if a dividend of 5 per cent. were paid, he became entitled to one-half per cent. on the gross takings. In 1927, when 5 per cent. was paid, his figure came up to £27,000, and in 1926, when they only paid a dividend of 4 per cent., he only got £3000. As I have said, that does not in any way relate to Mr. Morland so far as I know. I have not actually found the arrangement relating to Mr. Morland; but it does seem, whether a dividend of 5 per cent. or 50 per cent. was paid, or no dividend, it made no difference whatever to Mr. Morland.

**Sir PATRICK HASTINGS**—Not the slightest.

**The ATTORNEY-GENERAL**—The details entered in the accounts of 1926 and 1927 contain an item of about £2100 for auditor's fees, and I have very little doubt that part of that sum would relate to expenses elsewhere, and by no means all of that would go to Mr. Morland.

**Sir PATRICK HASTINGS**—Is it not better to make it clear he was paid 400 guineas?

**The ATTORNEY-GENERAL**—I am obliged. If my friend says so, I will accept that. So far as Mr. Morland was concerned Mr. Morland got 400 guineas, and whether the dividend was large or small it would make no difference to him at all.

[At this stage copies of the annual reports for the years 1921 to 1927 were handed to the jury.]

# Opening Speech for the Prosecution.

The Attorney-General

The ATTORNEY-GENERAL—First of all, look at the general balance sheet as at 31st December, 1926. It is headed: "Report of directors for the year 1926," and if you look at the balance sheet you will find the assets of the company appear on the right-hand side of the balance sheet, the total being £19,930,876. Now look at the liability side. The capital authorised is £25,000,000. Then you get the various preference stock and cumulative preference stock and the ordinary stock, which I have told you about—£8,800,000 they come to. Then you get the reserve fund. That is a fund which the company has built and which in due course the company may utilise and disburse for the advantage of its shareholders, and therefore it is treated as a liability, and it is £1,450,000. Then insurance fund, £1,300,000, and those added up come to £11,550,000. Then they set out the debenture stocks at  $4\frac{1}{2}$  per cent. and 5 per cent., which come to £1,400,000 and £3,100,000. Then debenture stock and preference dividends, dividends unclaimed, bills payable, sundry balances, accounts not closed, and debts owing from bankers, £2,864,440. The item "Sundry balances," which appears on the left-hand side, the liability side of the balance sheet, is an item which in the course of these various years I shall have to say something about. Just remember, if you will, at the present moment that there is in this balance sheet, as in many others, an entry of "Sundry balances." Then you get "Profit and loss account, £266,782." The balance sheet of course connects up with the profit and loss account. That comes into the balance sheet from the profit and loss account, and you will observe on the left-hand side there is this note.

There are contingent liabilities amounting to £4,000,000 for guarantees under the Trades Facilities Acts, and bills under discount by a subsidiary company and in respect of uncalled capital on investments.

That is signed by Lord Kylsant, and on the right-hand side you will find this note—

I report that all my requirements as auditor have been complied with, and that I have compared the foregoing balance sheet with the books of the company. In my opinion the balance sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company. I have verified the bank balances and have inspected the securities held for the investments which are valued under cost.

The important document in this case is the profit and loss account. This, you will remember, is a document which is laid before the general meeting, and just as the first document carried out the requirements of the charter, that the document must show the debts and assets of the said Corporation, here you get a document which is meant to comply with the requirements, that it has got to show the account of the profits made in the year. First of all, you will see it is called "Profit and loss account for the year ended December 31st, 1926." You bring in first of all: "By balance from 1925, £294,956, less dividend paid in June, 1926, £150,000, leaving £144,956." The next item is "Balance for the year, including dividends on shares in

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## The Attorney-General

allied and other companies, adjustment of taxation reserves, less depreciation of fleet, &c., £439,212; rent of properties, £38,900, and transfer fees, £116"—those three items come to £478,528. Then you will see transfer fees and transfer from reserve fund, and that totals up to £773,492 6s 8d. Now look at the other side of it. This is what they do with the money which has come in in that way. First of all they pay interest on their debentures, £218,000. The next thing they have to do with is interest and discount I do not know, but I rather anticipate that that is probably some interest they paid under the Trades Facilities Guarantee, or something of that kind. Whatever it may be, that again is a charge they have to make, and it comes to £55,209. Next in order come the preference dividends. They pay 5 per cent. on preference stock and 6½ on cumulative preference stock—that is £188,500. Now, if you look at the next, "Surplus in favour of the company," that is the surplus of the balance you have got from the other side; the total comes to £773,000 in favour of the company. They propose to utilise it by paying 4 per cent. on the ordinary stock, that is £200,000, and carry forward £266,000, so that you get a total of £773,492 6s. 8d., which squares with the right hand side.

Just look at that for a moment and ask yourselves what any ordinary person would infer from this document. I will consider the precise details of it at a later stage. You will see, in the first place, that there is at the bottom of the right-hand side an entry, "Transfer from reserve fund, £150,000," and you will observe that the company was paying the debenture interest—interest and discount, and the rate of dividend was 5 per cent. on preference stock and 4 per cent. on the ordinary stock, and you may think to yourselves: "Well, in the year 1926 I do not suppose things were very easy, but this company has got on fairly well; it is true it has drawn on reserves to the extent of £150,000, but, still, that is not so bad at a time like this." The facts were these: that instead of the transfer from reserve, which is there stated as being £150,000—instead of that being the amount of transfer from reserve—the amount transferred from reserve, or from items in no way relating to the year, was £900,000. There was a trading loss on the running of ships for the year of £540,206; and after bringing in interest on investments there was still a loss of £272,000, and this whole business, which purports to be the amount of profit made in the year and to show the utilisation of the moneys in the way I have indicated, was in fact only rendered possible at all because there had been a transfer from reserve, not of £150,000, but of £900,000. Instead of that document showing, as I am suggesting to you any ordinary intelligent man would read it as showing, that there had been a balance for the year of £439,212; in fact, there was a loss for the year of something in the neighbourhood of £300,000, because you only get that balance for the year of £439,000 by bringing into account £750,000, that is to say, the difference between the £900,000, which I have told you about, and the £150,000 here shown. You only get that balance by bringing into the year £750,000 which in no way ought to appear here at all.

# Opening Speech for the Prosecution.

The Attorney-General

I think it is fundamental in this case that you should acquire a plain understanding of what we mean by reserves, what reserves are, how they are accumulated, and when they can be used. I read to you a paragraph from the charter which sets out that the company can establish a reserve fund and use the reserve fund for various purposes, but it is not only this company or a chartered company which can establish reserves. Every company can establish reserves, and every well-managed company, if it possibly can, should establish reserves. To establish reserves you may put sums to a general reserve or put sums to an equalisation of dividend reserve, or a taxation reserve, or any reserve that you desire. In so far as you disclose those reserves no difficulty arises at all; and in these accounts I have called attention to we find disclosed in the balance sheet the reserve fund and insurance fund. There you have two disclosed reserves, and if you are going to utilise those reserves you are perfectly entitled to do so; but whenever you utilise the disclosed reserve you must show in the accounts that you have used it. If you are going to take from your general reserve a sum of money and put it into the profit and loss account, then you have to show it. The reserve fund before this year stood at £1,600,000. If you look at the general balance sheet as at 31st December, 1926, you will see the reserve fund there is £1,450,000. If you look at the same document the year before, you will find the reserve fund is £1,600,000, and of course, if you are utilising £150,000 of that reserve for the purpose of your profit and loss account the reserve which you disclose has got to come down. The reserve of £1,600,000 becomes £1,450,000. So far as disclosed reserves are concerned, there is no difficulty at all; the reserve is a general reserve, and the directors are entitled to use it when they like, but they have to disclose it. If it is a contingent reserve and is reserved for some contingency, when that contingency is over and past they are perfectly entitled to use it, and there, again, they must disclose it. But, members of the jury, reserves are sometimes not disclosed, and it is here the difficulty arises. See what that means. When I say "not disclosed," I mean not disclosed to the shareholders. Of course, reserves stand in the books, the reserves would be known to anybody closely concerned with the affairs of the company, to the accountant and auditor. If you look again at this general balance sheet for the year 1926, you will see that the reserves, if they are secret reserves, would be properly tucked away in that item, the last but one, on the left-hand side—"Sundry balances." If anybody were to ask you for the make-up, as it is called, of that figure £2,842,000, and he had the details of that figure, he would at once see that it is composed of certain reserve funds—disclosed therefore to the auditor, but not disclosed in the sense that no outsider reading the balance sheet could possibly tell whether there was or was not a reserve there. It is undisclosed in that sense. I have no doubt that it is by no means uncommon for a company in a given year to set aside out of its profits to what is called secret reserves, that is to say, without disclosing to the shareholders that it has done so. Perhaps



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## The Attorney-General

the business theory lying behind it is not far to seek. I suppose shareholders, like other people, suffer from the defects of human nature. It may be that shareholders are apt to be unduly elated by what is a mere temporary success and unduly cast down by what is a mere temporary loss. It may be the best policy in their interests therefore to smooth things out, to make the good years pay for the bad years. Still, as I have indicated that a secret reserve may be constituted, so equally I do not doubt that a secret reserve is by no means infrequently brought into a profit and loss account either to do away with, or to diminish a loss, or to turn a loss into a profit. But you may say: "Well, how does this square with the law, because the law says you have to make and publish fair and accurate accounts? How can it be accurate to say that you have only made £100,000, whereas in truth and in fact you have made £200,000? You have put £100,000 to reserve. How do you square it up?" There may be people, purists or theorists, who will say that the thing is wrong, that this building up of the secret reserve or the utilisation of the secret reserve in the profit and loss account of a year is wrong. They may say that, notwithstanding the manifest business advantages, both in securing the confidence of your shareholders and avoiding giving too much away to your competitors, you must bow to the general and wider proposition that on the whole it is wrong, that the directors or some of the directors should be in possession of information which shareholders know nothing about. Others would say that such a theory would be wrong, and they would say this: if you have secret reserves and are utilising reserves to profit and loss account, may it not be, paradoxical though it may seem, that by calling attention to a profit which is really an exceptional profit, which in no way reflects upon the profit-earning capacity, or by calling attention to a loss which is an exceptional, non-recurring, accidental, temporary loss, you may in fact, in portraying the thing as it were as a living whole, create a false impression? May it not be that the true view is that, so long as you are presenting a picture of the company as a living whole, as a continuous enterprise, so long as you clearly portray what is going on, there is no reason why you should show temporary and unexpected losses or why you should not diminish an unusual and unexpected profit? Whichever view is right, the arena of a Criminal Court is not the place to fight that out. Therefore I ask you to assume the view which is the more favourable view to the defendants. I may say that I am quite certain that no one who has ever held the office of Attorney-General would ever think of authorising a prosecution in a simple case where what was done was the building up of a secret reserve, or the use of a secret reserve in a profit and loss account; no one would ever think of complaining in such a case as that where it was used simply to iron or smooth out the ups and downs of business life. But obviously there comes a point at which the continued and deliberate and excessive utilisation of hidden reserves presents an untrue picture of the company, viewing the enterprise of the company as a continuous and continuing whole. One can imagine

# Opening Speech for the Prosecution.

The Attorney-General

a case arising—as in the case I am going to speak of here—of a shipping company, in the days of war making very large profits and accumulating a very large secret reserve, and thereafter steadily year by year making enormous losses, and notwithstanding the losses paying dividends, so that at last the time comes when it is quite obvious that unless something turns up, unless there is a completely new situation arising, that company is doomed. To present accounts and to utilise secret reserves in a profit and loss account, to make it appear that a business is going on smoothly and happily, when in truth and in fact that company is inevitably drifting on to the rocks, is, I submit to you, to present an absolutely untrue view of the company's prospects and the company's business, and is not to present a fair and accurate account as you have to do by law. And if it be said—and said it may be—"Well, but if once you admit that you have to draw a line, it is terribly difficult to know where exactly you are going to draw it," I think I would say this: "It is always difficult to know exactly where a line has to be drawn; but, notwithstanding that, you can very easily tell whether a case is on one side of the line or the other."

The case which I present to you here is a case in which you are only concerned directly with the accounts for the two years 1926 and 1927. What the prosecution say is this, that the accounts leading up to the year 1926 show that what was taking place was not a mere casual, unexpected, unforeseen or temporary happening, but that the situation which had been going on through these years was being developed and maintained in the year 1926, and that under those circumstances the accounts for 1926 were wholly false. If it is said that what was done in this case has been done before, do not be unduly impressed by that. Secret reserves have been built up and used before, I do not doubt for one moment. I am not complaining of the utilisation of secret reserves, but I do say this, that each case must be dependent upon its own circumstances. The cardinal point is that the accounts must reflect a fair picture of the enterprise as a living whole. You may smooth out the ups and downs, make temporary unforeseen losses disappear, and diminish exceptional profits, but you have no right to make an enterprise, which is a shareholders' enterprise, go down steadily, but surely, to disaster by letting it live for years on the profits which have been made long, long ago, without at least telling the shareholders what you are doing. That is why I am going to ask you to consider the accounts from 1921 to 1925, not, be it observed, that I am alleging any offence in respect of those years 1921 to 1925; I am not. I am not going to question the propriety of what was done in those years, but I am going to say that the consideration of what was done in 1921 to 1925 is of vital and critical importance to enable you to see the situation as it exists in the year 1926, and to ask you to say, having regard to that situation, that the accounts of the year 1926 failed to reflect a fair view of the company's enterprise and concealed from the shareholders that which it was manifestly the shareholders' right to know, and the duty of those who knew the facts

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## The Attorney General

to tell them. If you think that these accounts of 1926 and 1927 were published in circumstances such as I have indicated, you will, in my submission, come to the conclusion that those accounts were false, that they were false to the knowledge of the defendants, and they were published with intention to deceive and conceal the true facts.

At this stage I should like to show you Exhibit 21, a document which was kept by a gentleman whom I may call the chief domestic accountant of the Royal Mail Steam Packet Company. \*It was one, I think, put before Mr. Morland; Lord Kysant never saw this actual document. It is merely a convenient tabular method of showing the accounts of the company for the years 1920 to 1929. It would appear that the year 1920 was a very good year, and very wisely they hoarded their resources by putting aside out of the profits during the year a very considerable sum to reserve. You will see that the special debits included excess profits duty, corporation profits tax, new issue expenses, and premises reserve. Unfortunately it was the last of the golden years of prosperity. Then, that harvest being over, winter set in, and the next year, 1921, is the first of the bad years which continued. Instead of there being a surplus, there is now a deficit of £900,000, and, even after interest on investments is taken into account, there is still a deficit of £452,000. To meet that situation they utilised special credits, enumerated below, to the extent of £1,120,452. Utilising those special credits, you have got a surplus, as per printed accounts, of £668,400. If you look at the special credits down below, you see there are three items, bonus shares, Elder, Dempster & Company, £80,812; Nelson Line, Liverpool, £550,000; and Union Castle Company, £489,640. Those items were perfectly properly there, but they were in fact bonus issues declared by these companies, and the effect of that is this, that they were, as it were, capitalising their profits. Those three companies, having made very large profits in, I have no doubt, the war period, are at the present time capitalising those profits by making bonus issues. It is not that there is anything in the least improper in using them, but all one must say about that is this, and this is all that matters, that they are exceptional non-recurring items of income.

Before you pass from the profit and loss account for the year 1921, which contains the £668,000, notice, if you will, what is done with it. The debenture interest is paid, the preference dividends are paid, and for the rest the ordinary shares are paid 6 per cent., that is 2 per cent. interim and 4 per cent. is now paid, making 6 per cent. for the year. That is how the money is expended. Of course, as more than 5 per cent. was paid, Lord Kysant becomes entitled to his half per cent. of the gross takings, and he is entitled in respect of that year to £32,000 odd.

In the year 1922, after deducting running expenses, freights, general administration, repairs, insurance, depreciation of premises, &c., there is shown a deficiency of £570,840. Then you must take credit

\* See Appendix.



**The Attorney-General (Sir William Jowitt, K.C., M.P.)**

# Opening Speech for the Prosecution.

The Attorney General

for the investments which you have, £435,000, so you finish up with a deficit of £135,000. The special debits, which are referred to above, come to £120,175. Now come the special credits, special credits in excess profits duty—that is to say, a payment from the excess profits duty reserve of £100,000—war contingency reserves, £45,000; profit on sale of steamers, £271,000; and fleet depreciation fund, £440,000. In the prosperous times of the war various reserves had been built up, and one of the reserves that had been built up was called an excess profits duty reserve. You will probably remember excess profits duty was a thing which was payable in respect of seven years. The period of this company was the period of 1914 to 1921. The excess profits duty reserves had mounted to a figure of £2,200,000 of which one-half had been paid over and one-half had not. Of the £1,100,000 which remained on hand, £300,000 had been utilised for writing down investments. The fund therefore consisted of £800,000 in hand, but it also consisted of certain repayments which were made by the revenue out of the £1,100,000 which had been handed over. The reason that arose was in the war years there was a shortage of shipping, ships were being submarined right and left, and shipowners were induced by every means possible to build ships naturally to increase our tonnage. The people who built ships in the war years had to pay very high prices, and consequently it was considered fair in the case of shipping companies not to charge them the full amount of excess profits duty; but an arrangement was come to in 1922 between the various shipping companies and the Government that there should be what is called an obsolescence claim allowance, that is to say, over and above the ordinary depreciation very special regard should be had to the circumstances under which these ships had been built. The result of that was that of the £1,100,000 which had been paid for excess profits duty, roughly £800,000 was paid back, and therefore you see the excess profits duty fund, judging from the light of after-events, at the moment consisted of this £800,000 in hand which never had been paid over and £800,000 which was paid back, being part of the sum of £1,100,000 which had been paid over. The important thing to remember is this, that the reserve of excess profits duty had been built up in the war period, the last payment of excess profits duty being that £125,000 which occurs as a special debit in the year 1921.

The next reserve is the war contingency reserve, which was a sum of money put aside in the war because it was felt possible that officers of the Royal Mail Steam Packet Company who were serving with His Majesty's Forces might have some claim to the difference between their naval pay and the salaries they would have had if they had continued in the company. It never in fact materialised. They are taking £45,000 from that.

The next item of £271,000 is profit on sale of steamers. That, from the very nature of things, is again a typical instance of a non-recurring profit which is being brought in. I am not at all making any suggestion as to whether it is proper or improper to bring it into a profit and

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loss account. All I am saying is that it is obviously an item of a non-recurring nature.

SIR PATRICK HASTINGS—I am a little embarrassed by your saying that we need not consider whether it is proper or improper, because of course that may be material here. I understood you to say that the items in the year 1921 were not improper. Am I right in assuming, therefore, that there is no suggestion that these are improper?

MR. JUSTICE WRIGHT—The learned Attorney-General treats them as proper.

THE ATTORNEY-GENERAL—So far as I am concerned in this case, I am not challenging the propriety of any of these items in these years 1921 to 1925. The defendants are accused of nothing in respect of these years. All I am referring to these years for is in order that I may show the picture as it exists when we come to the year 1926.

The next item of special credit is fleet depreciation fund—the very large sum of £444,569. During the war a large number of ships had been lost, and when the payments made under the insurance contracts were received, if and so far as the payment received exceeded the amount at which any particular ship stood in the books, the difference was carried to a fund called the fleet depreciation fund. It differs from the other reserves technically in that this is not a reserve that appears on the left-hand side of the balance sheet. It was an item which appeared on the right-hand side of the balance sheet in that it would be an excess depreciation over and above the normal depreciation. It was again quite proper, as a matter of accountancy, to utilise it for the profit and loss account, but the relevance of it again is that, you will observe, it is a fund built up during the war, and that fund, so built up, is being brought into account to help the year 1922 as a special account. Those items, taken together—all of them, taken from war years and all of them at any rate of a non-recurring nature—amount to £860,000, and bringing those sums into account you will see that that £860,000 turns the debit of £135,364 into a credit of £725,000. If you will turn to the accounts for the year ended 31st December, 1922, and look at the profit and loss account, you will see that the profit for the year, including dividends on shares in allied and other companies, less depreciation of fleet, &c., was £725,300. You will observe on the left-hand side of the profit and loss account what they do with the money. Again, they first of all pay the £218,000 which they had to pay the debentures; the interest and discount come to £63,000; then, of course, they must satisfy their preference stock, £45,000 and £123,500. They have paid a dividend of 2 per cent. on the ordinary, and they are now going to pay a dividend of 4 per cent. That is to say, they consume £300,000 there, and the carry forward will make it £425,000 or £875,679. That is to say, in that year, in debentures and dividends, about £750,000 is consumed, and then of course there is interest and discount. In that year, like the last year, as the company paid a dividend of more than 5 per cent., Lord Kylsant became entitled to receive his half per cent. on the gross takings of the fleet, and accordingly in that year, 1922, Lord Kylsant received

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£23,376, that sum being embodied in the sum of £549,566, which is part of the general expenses of administration

Now, in that year again, unfortunately, there was a deficit. The deficit was not so bad as the deficit the year before, but you will observe that the insurance fund has very much decreased. Whereas in 1921 the amount expended on insurance was £426,000, in this year the amount expended on insurance is only £195,000. I should infer—I speak without knowledge—that that is in part due to the fact that war risks, which no doubt they had to provide for in the earlier years, are now passing away to some extent.

Mr JUSTICE WRIGHT—They were to some extent their own insurers?

The ATTORNEY-GENERAL—To some small extent—not the total loss. Then you will see depreciation of the fleet in the year 1922 was less than in the year 1921, £496,000; but of course that may again be accounted for by a sale of steamers. One cannot possibly regard that year as anything but very unsatisfactory, with a trading loss on the running of the ships at over a million pounds, even after bringing in investments of £135,000 and again a raid on reserve fund or special items to the extent of £860,000 in order to enable them to carry on business as usual.

Then we come to the year 1923, which was better than the year 1922. The figure you start with—that is to say, freights less running expenses—is now £1,063,000. Depreciation of fleet has gone up very considerably over 1922, and the trading deficit is now £443,000. Interest on investments is £422,000, and you are left with a deficit of £20,886. Of course it is not much good having a deficit of £20,000 if you have to pay £700,000 odd in interest and debentures. So they have brought in, by means of special credits, £800,000 from reserve funds; income tax reserve paid, £450,000; excess profits duty paid, £150,000; and deferred repairs paid, £250,000.

I must say a word about income tax reserve. From very early days and up to 1921 the fund amounted to £762,000. Now, that fund is not a static fund. If I may put it in this way, it is in the nature of a river rather than a reservoir, because it is augmented, and it is augmented automatically from time to time by reason of the operation of section 34 of the Income Tax Act, which provides that a trading concern, if it has losses in later years, may get back some of its earlier income tax. As the Royal Mail Steam Packet Company were having losses, they were within the region of section 34, and anything they got back under their section 34 claims would go of course to augment the income tax reserve. Secondly, it was augmented by this very simple procedure. As the Royal Mail Steam Packet Company were making losses, they were no longer liable to pay any income tax. On the other hand, the Royal Mail Steam Packet Company, in paying their dividends, would of course deduct tax. Consequently, the amount which they deducted and the amount which they did not have to pay over to the Revenue would automatically swell the income tax reserve. The income tax reserve was reduced, on the other hand,

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by this consideration: as and when repayments of excess profits duty were made, by the law of the land a repayment of excess profits duty is deemed to be income of the year in which it is repaid. They would of course use that fund for the payment of income tax which arose out of the repayment of excess profits duty. Broadly speaking, that is the history of the income tax fund. You may take it that it was £760,000 in 1921, that it was augmented by the more or less automatic methods that I have indicated, and it was utilised for the purposes that I have also indicated. In that year we find that £450,000 is taken from the income tax reserve.

The deferred repairs fund was a fund which arose during the war by reason of the nature of things, the necessity of turning tonnage round quickly, and the absolute necessity of not filling up our ship-building yards, if it could possibly be helped. The repairs would have to be done in the future, and consequently a reserve was constructed for that purpose, amounting to £800,000. Repairs done in 1920 and 1921 amounted to £400,000, and so you get a reserve of £400,000 left over. The only thing to notice about these complicated facts, I think, is this, that that again was a war reserve. It was a sum that resulted from the wise policy of putting things aside during the war period, and £250,000 is taken from that. So that you get £800,000 of items relating to the year brought into the account to enable the company, notwithstanding its deficit of £20,000, to pay its debenture interest and its dividend.

If you now look at the profit and loss account for the year ended 31st December, 1923, you will see: "By balance from 1922, £325,000, less dividend paid in June, £200,000." Now the balance for the year, including dividends on shares in allied and other companies, less depreciation of fleet, &c., is £779,114 7s. 11d.

**MR. JUSTICE WRIGHT**—That is a change in expression, is it not?

**THE ATTORNEY-GENERAL**—Yes, it is interesting to see, and it is important that you should realise it. The expression in 1921 is called "Profit for the year," and it is now "Balance for the year." Now, see how they expend this £779,114. After paying debenture interest, preference dividends, and interest on the ordinary shares, they have £130,000 to carry forward. In that year again, as a dividend of more than 5 per cent. was paid, Lord Kylsant becomes entitled to his half per cent. on gross takings, and in 1923 he received £26,045. Members of the jury, this was the third year running in which there had been a deficit.

1924 was no better than 1923. The figure you start with, freights less running expenses, slightly less than the previous year, is £962,000, and there follow the figures for the general administration, repairs, and insurance fund. That is substantially down. Depreciation of fleet is substantially up. Then you have depreciation of premises, special debits enumerated below, a total of £1,400,000, which shows a deficit again at this time of just over half a million pounds. The deficit for 1924 is £500,000, and if you deduct the investments you have a deficit of £93,000. In this year, in order to keep the pot



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boiling, if I may use a homely phrase, they are using £870,000 of special credits in no sense relating to this year, and if you look at the account you will see how it is dealt with there. The balance, you will remember, is brought forward in the usual way. "Balance for the year" is the phrase used now, and, including dividends on shares in allied and other companies less depreciation, is £772,829. That is the figure you get after you have brought in £872,000 special reserve. As the company earned more than 5 per cent. on its ordinary shares, Lord Kysant became entitled to a half per cent. commission on the gross takings; that is to say, his share came to £26,495.

Now I come to the last year, and I want to examine, with regard to this, the pre-1926 period. Gross earnings less running expenses are put at £880,000. Then there was administration and repairs, insurance fund, depreciation of fleet, depreciation of premises and special debits, £1,450,000, with a trading deficit of £570,000, bringing the dividends, which are not so high as they have been, to dividends of £261,000. This year you have a deficit on doing that of £309,105. Then you have to bring in special credits, and see what you do. You bring in excess profits duty, £300,000; income tax reserve, £200,000; and investment profit, Nelson Line, £490,290. The Nelson Line went into voluntary liquidation, and the liquidators disposed of its assets. The sole shareholder was the Royal Mail Steam Packet Company, and that £490,290 represents what the liquidator paid on the winding-up of the company over and above the figure at which the Nelson Line stood in their books. It was in the nature of a special item; it cannot recur again, and it is a thing made use of to swell the profits of the year 1925. Now, if you will look at the balance sheet for the year 1925, you will see how it is dealt with.

Sir JOHN SIMON—I am not quite clear whether the view of the Crown is that that sum was or was not the proceeds of the year 1925.

The ATTORNEY-GENERAL—I will answer if Sir John likes, but as the defendants are not charged with anything irregular in respect of those years 1921 to 1925, and as I am only saying it is setting the scene for the year 1926, I have deliberately said what was done in that year.

Mr. JUSTICE WRIGHT—I think what the learned Attorney-General means is that he is raising no question about it, and he is making no criticism in the sense that he is not raising any charge or any complaint in these proceedings in respect of anything done in these years.

The ATTORNEY-GENERAL—That is precisely the position. If you look at the profit and loss account for the year 1925 they bring forward a balance from the year 1924. Now see this phrase: "Balance for the year, including dividends in shares in allied and other companies, adjustment of taxation reserves, less depreciation on fleet, &c., £731,103." There is a new phrase there—it is in small print, you will notice—"Adjustment of taxation reserves." The dividend for this year is 5 per cent. instead of 6 per cent., which it has hitherto been, but 5 per cent. is the figure which entitled Lord Kysant to receive—as he did receive in respect of that year—the sum of £27,165.

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May I just ask you to consider with me what those five years show. During those five years, 1921 to 1925, the following sums have been taken from reserves—Excess profits duty reserve, £830,000, income tax reserve, £1,050,000; war contingency reserve, £45,000; corporation profits tax reserve, £40,000; fleet depreciation fund, £444,000—making a grand total for the utilisation of reserves, which I may substantially call war-time reserves, of £2,800,000. The story does not end there. In addition to drawing on those reserves to keep those going over five years, they have had recourse to non-recurring items; for instance, bonus shares of Elder, Dempster; bonus shares of Nelson, Liverpool; bonus shares of the Union Castle; and the investment profit on the winding up of Nelson, Ltd., of £1,600,000. The total is £4,400,000; but I think it right in considering the figure to take off from it the amount of the special debits, £400,000, and you get this result. To carry on and to pay dividends and so on in those years this company utilised from its reserves £4,000,000. The story does not quite end there, because running through each of those five years you will see a figure called "Interest on investments." You will remember it started at £400,000, and in the last year, 1925, it was £261,000. In order to get the picture of the prospects of this company one wants to realise how far that "interest on investments" is likely to continue. If, for instance, "interest on investments" were being paid by companies that were doing exactly the same as the Royal Mail Steam Packet Company was, it is obvious you could not rely on those investments going on very much longer. There is no doubt but that a substantial part of those investments was derived from 100 per cent. subsidiaries, and here you have another fact which would be unknown to Mr. Morland, but would be known to Lord Kylsant. I do not pretend to go through all these subsidiaries, because it would be too complicated, but I will take the largest of the subsidiaries—and I frankly say that this is the gravest of the subsidiaries. I will give you, if I may, the figure relating to the Pacific Steam Navigation Company, which is itself a chartered company. In 1921 you will see there is a deficit of £735,000 and a dividend of £63,000. That dividend of £63,000 was of course paid to the Royal Mail Steam Packet Company. The next year you see a deficit of £251,000, with a dividend of £67,000; the next year a deficit of £416,000 and a dividend of £57,000; the next year a deficit of £242,000 and a dividend of £58,000; and the next year, 1925, a deficit of £298,000 and a dividend of £60,000. The sum total of those figures is this, that so far as that company is concerned, during those five years 1921 to 1925, its deficits were £1,600,000, or, as I prefer to take it, £1,300,000, because I think it is fair to deduct those red-ink figures, and its dividends were £300,000. Now, it is quite obvious that if you expend in five years £300,000 in dividends, and at the same time your deficits come to £1,300,000, though you might have a merry life, you are probably going to have a short one, and anybody knowing the situation so far as that subsidiary was concerned would know this—going back to the Royal Mail Steam Packe

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Company's accounts—it would be rash to regard a continuance of that dividend of £60,000 as something which would continue in the indefinite future. So over these five years you have those £4,000,000 utilised in the way I have indicated, and you have got substantially £3,900,000 expended in paying debentures, discount, preference shares always paid in full, and the ordinary paid at least 5 per cent.; and you have during those five years Lord Kysant drawing in all a total of £135,000, notwithstanding this utilisation of this very large quantity of reserves. It may be said these figures depend to a certain extent on depreciation. If you have depreciated too generously, or if you have made too generous provision for insurance, then the results would be less unfavourable than they would appear to be when you look at this document. That is quite true. I am not in a position to say whether there was over-depreciation or over-insurance. Depreciation was normally taken on twenty years' life; but make what allowance you like, if indeed there is any evidence of that sort, it is quite obvious that that company had had five disastrous years, unless a turn in the tide came soon that company would go down if it went on paying dividends on its ordinary shares or even on its preference shares.

Before I pass from this 1921-1925 period, you may think it not an unimportant fact in this case that that word "balance" is used, and I make this suggestion about it. First of all, why was it that the word "profit," which had been used in 1921 and 1922, became "balance"? One would suppose that whoever was responsible for these accounts was not very happy about putting in the word "profit." Does the word "balance" really make any difference? My submission to you is this, that that word "balance" was very carefully selected so as to arouse no suspicion in the mind of the ordinary man who saw it, who would not notice it or think anything about it, and at the same time it was a word which enabled those who put it forward to say, if it ever became necessary to say it: "Oh, we never said there was a profit; all we said was there was a 'balance.'" I suggest that no ordinary person would draw any distinction between the phrase "balance for the year" and "profit."

With regard to the history of the phrase "the adjustment of taxation account," which comes in for the first time in the year 1925, in Exhibit No. 24 which came from Mr. Cason, who was head accountant of the Royal Mail, you see what he says: "Mr. Morland has signed the balance sheet"—that was the balance sheet of the year 1925—"subject to your approval of an alteration in the profit and loss account as per rough proof attached. If you will be good enough to let Mr. Marshall telephone me to-morrow morning that the alteration is approved, copies of the report should be available about the usual time." Well, now, unfortunately the "rough proof attached" is lost, but Mr. Cason says that the alteration which was there being made was the putting in of the words "Adjustment of taxation reserves." He was not wanting to sign the balance sheet without these words. In my submission to you that phrase "adjustment of taxation reserves" was

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a phrase quite deliberately prepared and selected and chosen as a phrase which would convey nothing whatever to the mind of the ordinary person, but at the same time would enable anybody to say, in case the need thereafter arose: "Oh, but all this is covered by the phrase 'adjustment of taxation reserves.'" It betrays, in my submission to you, an uneasy conscience about what was being done. Looking at the balance sheet for 1925, you see the last item but one is "Sundry balances," and that is the item in which most of these items were—"Sundry balances; accounts not closed; and debts owing to the company, &c, £2,602,000." Do you remember that in the good old days of 1921 sundry balances stood at £6,200,000? Of course, you cannot say that the difference between these sums is entirely accounted for by the utilisation of reserves, because there are other factors that come in which disturb the equilibrium, but, broadly, you can say that the very heavy utilisation of reserves is reflected in that difference, this company living on its own fat was very rapidly becoming a skeleton.

In October, 1926, Lord Kylsant told Mr. Cason to prepare an estimate because he said he wanted a forecast of how 1926 would look, and added the significant words: "and what reserves we have available to meet any deficiency." That illustrates rather well the type of mind of a person who is going in for what is euphemistically termed "adjustments." Accordingly, Mr. Cason, the head accountant, prepared a document which is Exhibit No. 6. The first thing you notice is that at the bottom left-hand corner it is marked "12th October, 1926, shown to chairman," and the document shows this, taking the right-hand side: "By voyage account; receipts less expenses, £26,500; by sundry receipts, including interest on investments, £350,000; and by deficiency (excluding dividends on ordinary stock), £1,100,000." That balances up to £1,476,000. Then on the other side there is: "To debenture interest, £218,000"; there is a preference dividend of £233,000; there is the insurance account; there is depreciation of fleet, &c.; and there is interest and discount, £50,000—£1,476,000. Now that is on the basis of a deficiency of £1,100,000, and that deficiency is on the basis of no payment at all being made on the ordinary stock. If you are going to pay a dividend of 4 per cent. on your ordinary stock, it will take £200,000, and that will increase your deficiency from £1,100,000 to £1,300,000. You see written out on the right-hand side the following figures which Mr. Cason wrote there on the instructions of Lord Kylsant:—"Unpublished reserves, £600,000"; then, "Query from insurance premiums, £100,000; carry forward, £144,900; investment depreciation reserve, £300,000; and bonus shares from Nelson, £200,000." Written down in smaller writing you will find out how that £600,000 is made up in the bottom left-hand corner—some strange writing which obviously I should infer referred to excess profits duty reserve.

Mr. Justice Wright—This is a document which only affects Lord Kylsant. It will have to be proved whether it is evidence against both or evidence only against him.

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The ATTORNEY-GENERAL—Mr. Morland would never see this document, as far as I know. It was a document prepared in the office. It is not an account; it is a mere estimate, made up in October, 1926, before the year is up, and it can only be a guess, but it does show that Lord Kylsant estimated a deficiency of £1,100,000, even apart from any dividends at all, on the ordinary shares. Lord Kylsant had told Mr. Cason that he was going to take a bonus of £200,000 from Nelson, but for some reason or other that was cancelled, and although the bonus of £200,000 was passed through the books of the Royal Mail Steam Packet Company it was at a later date cancelled and taken out of the ledger, and the £200,000 never did in fact figure in the profit and loss account at all. As the £200,000 Nelson bonus disappeared Lord Kylsant told Mr. Cason to take an extra £200,000 from excess profits duty reserves. That is a pretty good illustration of adjustment. Before I reach the end of the year 1926 I want to warn you quite clearly that there is no evidence to connect Mr. Morland with this. Mr. Fisher, who is the general manager of Barclays Bank, at the head office, wrote to Lord Kylsant on 3rd December, 1926—

With reference to your recent interview with the chairman, and your letter of the 30th ultimo, we have pleasure in informing you that it has been agreed to grant the Royal Mail Steam Packet Company an additional £200,000 on overdraft, making £500,000 in all; and we gather it is your intention to repay this additional advance within the next three months from the proceeds of a public issue. May we express the hope that when the time arrives we may be able to assist in the issue which is to be made.

Now, it is in my mind a matter of very great importance in this case that you should bear in mind when you look at this 1926 account, the document which comes to be published in the year 1927, that Lord Kylsant has in his mind at that date the desirability, and he has apparently given some undertaking, or at any rate a statement of his intention, to have a public issue. I think you will readily agree that a public issue would be much more likely to succeed if you could dress up the accounts of 1926 in a favourable garb. The Royal Mail Steam Packet Company might have had some difficulty in going to the public and asking the public to subscribe to a public issue if they had said. "We ought to tell you that, though we have built up large reserves in the war time, in the last five years we have used £4,000,000 in payment of debenture interest and dividends on our stock."

Then steps are taken to prepare a profit and loss account for the year 1926. Amongst the various items detailed in Exhibit No. 7 you will see: excess profits duty, £550,000; income tax reserve, £175,000; investment profit in Nelson Line, £25,000; and the disclosed reserve of £150,000. All that is put before the auditor, but what is put before the directors? Because, after all, although Lord Kylsant is chairman, he is not alone in this matter; he has got his brother directors. The document put before the directors is Exhibit No. 13, in which there is nothing to disclose any utilisation of any secret reserve at all. The transfer from the published reserve fund of course is disclosed, but there

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is no other disclosure at all made to these directors, and it is right I should say that, so far as any figures in our possession go, so far as I know, no document ever was put before them showing that there was any transfer from the secret reserve.

I would again ask you to look at the profit and loss account for the year ended 31st December, 1926. You will not find there anything whatever about the transfer of the hidden reserves, although, as we know now, those transfers amounted to £750,000 over and above the £150,000 which is disclosed. The only way in which, perhaps, you can get this into the balance sheet and say they are disclosed—if it is to be suggested that they are disclosed—is if it is said they come under the phrase: “Dividends on shares in allied and other companies; adjustments of taxation reserves.” That is a phrase which in my submission would convey nothing to the mind of any ordinary man. Whether there is supposed to be a distinction between a transfer from reserve of £150,000 and an adjustment, I do not know; but can you imagine any person reading this balance sheet and seeing that you get a transfer from reserve fund of £150,000 suspecting that the transfers from reserve fund were £900,000? In my submission that balance sheet was a false balance sheet; it made it appear that there was a balance for the year of £439,000, whereas that balance was only arrived at by bringing in £750,000 which did not relate to the year. What is the good of talking about a balance for the year when in truth and in fact there was a loss for the year of £300,000? The statement on the accounts and balance sheet which Mr. Morland signs, as I have indicated to you already, is that it exhibits in his belief a true and correct view of the state of the company's affairs. The dividend this time, you will observe from the profit and loss account, is only 4 per cent., and indeed, in view of the fact that the company are at this time drawing on the disclosed reserves, it would hardly have been possible to have paid a dividend of more. Of course the result of paying a dividend of only 4 per cent. is that Lord Kylsant has to be content with the £3000 which his agreement entitles him to in respect of this year, there not having been a dividend of 5 per cent.

With this statement of accounts there is presented to the shareholders the report of the court of directors, and this document again is not a document in which Mr. Morland is responsible; it is a document in which Lord Kylsant is responsible.

The court of directors submit herewith the audited accounts of the company for the year ended 31st December, 1926. After providing for depreciation and taxation, there is a balance for the year of £478,535 13s. 4d., to which is added the credit balance brought forward from the accounts for 1925 and £150,000 transferred from reserve, making a total of £773,498 6s. 8d., out of which debenture and other interest and dividends on preference stocks to the end of the year have been paid. Looking to the abnormal industrial conditions which prevailed at the time, the court of directors considered it prudent in October last not to pay any interim dividend on the ordinary stock, but they now recommend a payment of dividend on that stock of 4 per cent., less income tax, for the year 1926, leaving a balance of £66,782 9s. 2d. to be carried forward. Dividend warrants will be posted to the holders of ordinary stock on 31st May.

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There is nothing further in this document I wish to draw your attention to until you get to the last paragraph but one. I notice "Mr. Harold J. Morland, F.C.A. (of Messrs. Price, Waterhouse & Co.), offers himself for re-election as auditor." He offers himself for election by the shareholders as their auditor charged to see that their interests are being duly safeguarded. This is the sixth year running in which there has been a shattering loss, and in this year £900,000 is being taken from their accumulated fat, if I may use a vulgarism. They are only telling the shareholders about £150,000. They are giving them no clue, no hint, unless this carefully prepared language seems to you to be any hint, that there is anything wrong.

SIR JOHN SIMON—Would you mind my calling your attention to a passage on the third page of the report near the bottom of the page, commencing "For the first four months of 1926?"

THE ATTORNEY-GENERAL—Sir John suggests I should read this, and I am only too glad to read it.

For the first four months of 1926 there was a considerable increase in the quantities of outward cargo compared with the corresponding period in the previous year, but the outbreak of the General Strike and the prolonged coal stoppage subsequently had an adverse effect upon shipments from this country, postponing the recovery in trade and shipping.

Now, that is quite accurate. At the same time you will notice the third paragraph of the document that I read. One would infer from that paragraph that the cloud which was there in October had rather passed away. They say—

Looking to the abnormal industrial conditions which prevailed at the time, the court of directors considered it prudent in October last not to pay the interim dividend on the ordinary stock, but they now recommend the payment of a dividend on that stock of 4 per cent.

Well, that is the year 1926. Sir William M'Lintock was called in, and probably, if he could have had prophetic instinct, he would most certainly, I suspect, have avoided taking on the job. "I have gone into the year 1926," he says this, and as this tells in favour of the defendants I think it right I should say it. He thinks that in the year 1926 they were over-generous in their insurance and over-generous in their depreciation, and he thinks, to cut a long story short, they make the picture for that year £100,000 worse than they need. So that he would say, if I follow it rightly, that instead of there being a deficit of £272,000 there should be a deficit of £172,000. Profit and loss account for the year ended 31st December, 1926, showed a published profit of £478,535; but there were items not relating to the year brought in other than the £150,000, and consequently I say, instead of there being a profit, there was a deficit or loss on the year of £272,000, if you accept the one set of figures, or £172,000 if you accept the other; but the deficit is arrived at before they have to find the money to pay the debentures.

Again I want to tell you something about the subsidiaries. If

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you look at the long table you see for the year 1926, they receive in interest on investments £267,965. The position of the dividends was as follows:—A large portion of the £267,965 is dividends received from the 100 per cent subsidiaries. So far as the Pacific Steam Navigation was concerned, they paid their usual dividend of £60,000 and sustained, I am afraid, what I may now call their usual loss of £163,000. Meat Transports paid a dividend of £49,000, though they had a loss of £21,000. The Nelsons, the one bright spot at this stage, paid a dividend of £42,000, having made a profit which entitled them to do it, namely, a profit of round about £80,000. Treating them as a whole, in 1926 the 100 per cent. subsidiaries paid a dividend which is substantially half of the £267,000, although they sustained between them a deficit of £213,000—obviously again a state of affairs which could not go on for very long, and one which it is material to consider if you are endeavouring to portray a true picture of the company's affairs.

Coming to the year 1927, the first thing I have to do is to ask you to look at Exhibit No. 28. Bear in mind that this does not affect Mr. Morland. It is headed: "Memorandum for the chairman; Barclays Bank overdraft."

On my calling at the bank in connection with the continuation of the above, Mr. Fisher was not available, but I saw Mr. Greenwood, the town manager, whom I have usually seen. He called to remembrance that it had been agreed for a new issue to be made to clear off the overdraft, and could only at the moment agree to extend the overdraft for a further three months, when the question can again be gone into. I imagine that the bank may be disappointed because two White Star Line issues have been made in which their services were not required, as was the case in the last issue of our preference stock.

So there again, remember, when we come to consider the make-up and build-up of the accounts of 1927, this is rather more definite than it was the year before. There had been a suggestion about it the year before, and this time the manager is calling to remembrance that an agreement was made to clear off the overdraft. The significance of that is clear. Any business man or woman would understand that the result revealed by the accounts would obviously affect the terms upon which they are borrowing money. This year, as in the previous year, before the end of the year, Lord Kylsant instructed Mr. Cason to prepare a preliminary statement to see how the thing would look. Exhibit No. 14 was shown to Lord Kylsant by Mr. Cason, and Lord Kylsant told Mr. Cason to take what was necessary. That document was not shown to Mr. Morland. Now, to take what was necessary to pay a 5 per cent. dividend must occur to anybody to be unfortunate. Here is a man who, whenever a 5 per cent. dividend is paid, becomes entitled to a very substantial remuneration over and above the last year when it was 4 per cent. This is the seventh consecutive year with losses, and yet Lord Kylsant was telling Mr. Cason to take what was necessary. It is an interesting sidelight again on what these words "adjustment of taxation reserves" would cover. Mr. Cason takes this thing away, alters it as it now appears in red ink, and brings it back to Lord Kylsant



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in the red-ink form. You see considerable alterations had become necessary. The first item on the right-hand side, £433,000, has come down to £185,000, simply because, as I follow it, £247,000 has gone out from the other side of the account. Then sundry receipts and rents he is able to estimate more closely at this date at £85,000 instead of £70,000. Bonuses remain the same. Dividends from investments are slightly down. The net result was a total of £1,400,000. Those figures were shown to Lord Kysant, and Mr. Cason got Lord Kysant's approval of what he proposed to do, and down to that point Mr. Morland has nothing to do with this document at all; he never saw it. Then Mr. Cason takes a document to Mr. Morland. That document has now been lost, but it was a document which showed what transfers from reserves were being put through in that year. He takes it to Mr. Morland to get his approval, and Mr. Cason says to Mr. Morland, "I do not like it," and Mr. Morland answers, "Nor do I." Notwithstanding the view which Mr. Morland expressed, as you will see he signs the document. The document corresponding to the document in the other case in 1926 is Exhibit No. 15. The result of that year's trading was this, the profit—that is to say, the gross earnings on land, trade, profit on ships, and so on—this year amounted to £972,000. That is better than it has been for some time, since 1923. Then there comes the general administration, general repairs and maintenance, insurance fund, depreciation of fleet, and depreciation of premises, £1,300,000, and you get a trading deficit of £334,000. Then comes interest on investments, and you will see how this sum is swollen this year. The interest on investments is now £559,000. It has never been anything like that for the last few years; that is because there is the bonus on Nelson's of £325,000, and that leaves you with a surplus of £224,000; but of course a surplus of £224,000, even assuming you have got it, and that it is real, would not be enough to enable you to pay debenture interest and interest charges, let alone anything on the shares. £512,000 is taken up in the form of special credits. Let us see what they are: Excess profits duty is £232,788; income tax reserve is £120,000; and profits on steamers and premises, which were divided as follows, £18,000, I think, for steamers and £90,000 for premises. That was brought in as a credit for the year to profit and loss account. Then corporation profits tax amounted to £32,905. Then there were butter freights and Government charter reserves. I do not know what those are, but that was another reserve being exhausted. In this connection I think you ought to see the statement that was laid before the directors, Exhibit No. 19, which is headed "Statement of account for the year ending 31st December, 1927." Nothing whatever is said about any transfer from reserves.

Now, will you look at the profit and loss account for the year ended 31st December, 1927? You bring in the balance from 1926 and the dividends paid in 1927, and then you have the balance for the year, including dividends on shares in allied and other companies—adjust-

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ment of taxation reserve, less depreciation of fleet, £697,000; rents of properties, £39,000; transfer fees, £475, totalling some £737,292. Now see how they expended the money: Debenture interest, £218,000; interest and discount, £29,412; dividends on preference stock, £45,000, and £118,000 surplus in favour of the company. Then 2 per cent. dividend was paid in November, 1927, on ordinary stock, £100,000, and proposed to be paid 3 per cent on ordinary stock, £150,000; carried forward, £73,000; or a total of £323,000, balancing at £804,000. That is what they did with this money which they got from these sources, and as the dividend is once more restored to 5 per cent it is apparent, there being no disclosed transfer from reserve as there had been in 1926 when there was a disclosed transfer of £150,000, with a dividend down to 4 per cent., the dividend goes up to 5 per cent., Lord Kysant getting £26,842, being his half per cent commission on the gross takings, in view of the fact that the company has paid a dividend of 5 per cent. Now, what does this account show? This account, on the face of it, to any ordinary reader shows this: it shows that you have on the right-hand side, the credit side of your profit and loss account, in addition to the carry forward from 1926 a profit of £737,000; but in fact we now know that you only arrived at that figure by transferring £512,386 either from reserves or at any rate from non-recurring items. You have a profit for the year of £224,000 instead of £737,000; that is to say, you have a profit insufficient to pay the first two items on your liability side of your profit and loss account and insufficient to pay interest and disbursements. Sir William M'Lintock, who has gone into these figures carefully, thinks that in this year, like the rest, when he is in their favour, they have under-depreciated to the extent of some £40,000, and over-insured to the extent of £10,000, making a balance of £31,000; but after all £31,000 is a small matter compared with what you are dealing with here.

What about the receipts from subsidiaries for the year 1927? The Pacific Steam Navigation we can easily deal with, but it paid its dividend of £60,000 and sustained its usual deficit of £160,000. The Meat Transport paid a dividend of £49,000, and they made a profit of £28,000. The two Nelson Companies, so far as their dividends are concerned, paid a dividend of £6000 with a profit of about £38,000, in this figure which you see here as interest on investments of £559,000, and you will remember that the make-up of that is that that includes this £300,000, the bonus from the Nelson.

And here I must explain to you a most extraordinary story. You may think whatever the technicalities or rights and wrongs of the thing are, it is very pitiable that a great enterprise of the city of London, controlling this vast interest in shipping, is resorting to the sort of finance which, what I am going to indicate to you in a moment, would lead one to suppose. You will remember that the Royal Mail Steam Packet Company owned the entire shareholding in H. W. Nelson, Ltd., and the Nelson Steam Navigation, Lord Kysant

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being chairman of both of those and of the Royal Mail. The first idea was this: let the two Nelson Companies declare a cash bonus of £300,000, £200,000 for one of them and £100,000 for the other. That, of course, would have the effect of helping the Royal Mail accounts very considerably. It might have been at that time, and probably was, very inconvenient, if not impossible, for the Nelson Companies to find the cash to pay the cash bonus. So that the Nelson Companies could declare a bonus of £300,000 this was arranged. The Nelson Steam Navigation Company had £1,000,000 of share capital authorised but not yet issued. How would it be if the Nelson Steam Navigation Company issued their at present unissued capital and the Royal Mail Steam Packet Company subscribed and purchased it? So that was arranged. The Nelson Steam Navigation Company were to issue £1,000,000 at par, and the Royal Mail Steam Packet Company subscribed for those shares, but one-half of them were to be taken fully paid; that is to say, half of them involved the payment of £500,000, and, with regard to the other half, they were to be 10 per cent. paid. That would involve the Royal Mail Steam Packet Company paying to the Nelson Steam Navigation Company £550,000, £500,000 at par and £50,000, if they paid 10 per cent., would be the sum on the other £500,000. All those steps are going to take you back exactly where you were to begin with. The first step is that Nelson declared a cash bonus of £300,000; the second, the Royal Mail Steam Packet Company go through a procedure which makes you think they owed Nelson Steam Navigation £550,000; and the third step—and this is perhaps the most ingenious of the lot—was: they said, "As we have to square this up and find another £250,000, let us sell our shareholdings in H. W. Nelson to Nelson's Steam Navigation and that will mean £250,000 there." Well, that all means really nothing. The Royal Mail Steam Packet Company already owned the entire shareholding in H. W. Nelson and Nelson's Steam Navigation Company, and whether the capital of Nelson's Steam Navigation Company is one hundred, one thousand, one million, or one billion shares it does not matter: it owned everything there was to own so far as shares were concerned. Neither does it matter if you have two companies and own the entire shares in each, the entire shares in H. W. Nelson and the entire shares in Nelson's Steam Navigation Company—it really does not matter whether you sell one to the other, or the other to one. But those complicated steps are taken: the declaration of a bonus by Nelson's of £300,000 and the subscribing for shares by the Royal Mail in Nelson's new issue of £250,000, and the sale by the Royal Mail to Nelson's of the shares in the other Nelson for £250,000, the net result being all square, you are where you started, except that you get the credit in your profit and loss account of £300,000. You have got something which makes things look better to the tune of £300,000 than the way they looked before. That accounts for the fact that in this year, 1927, instead of the interest from investments being as it had been in 1926, £260,000 odd, it is £559,000. Now let us look at these facts together

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for a moment. In 1926 and 1927, of the 100 per cent. subsidiaries that paid dividends or contributed to these investments, there was shown in dividends and bonuses, including the Nelson Companies, £576,000, notwithstanding that in those two years these same subsidiaries lost £383,000. That is the position with regard to the year 1927.

[At this stage the Attorney-General read the directors' report for the year 1927.]

Let us try and bring this thing to a focus. It seems to me it comes to this: in the years 1926 and 1927, including the £150,000 which they showed as transfer from reserves, and which therefore becomes part of the profits, the published profits were £628,535 in the one year and £737,292 in the second year. They did not disclose transfer from reserves of £900,000 in the one year and £500,000 in the other year; that is to say, they did not disclose transfers which amount to more than the entire profits they showed for the two years, and they did this after a five-year period in which they had utilised and not disclosed some £4,000,000 either from reserves or non-recurring items. So far as Lord Kylsant is concerned, each of these accounts for 1926 and 1927 is published after he knows and has made up his mind that he is going to the public for a fresh issue. How can that be justified? Is it to be said that secret reserves have frequently before now been brought into a profit and loss account? I do not doubt that they have. Is it to be said that they have been brought into the profit and loss accounts in circumstances comparable to these circumstances, namely, where you have had this long continued succession of failures? Well, I hope not; but supposing they have. If this is done a hundred times it does not make it any better. If you think these documents are false, if you think there was on these documents any intention to deceive the shareholders, no matter what the motive may be, it does not make it a bit better that it has been done in a lot of other cases, even if the circumstances in those other cases are comparable circumstances. As I say, I sincerely hope not. Is it to be said that, as you go through these accounts, you find that the accountancy is perfect, nothing the matter with it? One would expect that. Members of the jury, the matter in this case is not accountancy; what was wanted was a little more disclosure. Is it to be said: "Well, after all, was not this the right principle, was it not right that we should put a brave face on things, that we should continue to carry on, keep our name before the public, be ready when the better times come, as come they surely will, to take advantage of those better times? We have only got to have an increase of, let us say, 10 per cent. or 20 per cent. in the price of freights, or in the volume of our carrying trade. Was it not a good gamble to go on?" Well, I am quite unqualified to express any opinion about the business of it, but I do know this, that the law says that you may not publish a false document with intent to deceive, and whatever your view may be about the desirability of carrying on and not letting people know your difficulties, you have got to stop short of

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false documents. With regard to the argument, if argument it may be, that may be advanced: "Well, was it not a good gamble; was it not a long shot to go on, worth trying?" I would say this, that unhappily that dock is frequently peopled with optimistic gamblers who gambled with other people's money. I ask you to form the opinion that the company had long passed out of the period of little temporary ups and downs when you could utilise the fat you had gathered up in the good old years to pay for the troubles of to-day. This was the salient fact that must have been present to the mind, certainly, of everybody concerned in the year 1927. "Unless things get better, and get better promptly, this company of ours is going to disaster." That was the position; it is no good not facing it. By 1926 and 1927 they had drawn another one and a half millions of the reserves, which added to the four millions made five and a half millions, and there was precious little left in the company in the way of secret reserves at the end of 1927. Five and a half millions had gone in the seven years, and in the year 1927, without telling the shareholders, the court of directors declared a dividend of 5 per cent. on the ordinary stock, and Lord Kylsant takes a commission of a half per cent. on the gross turnover. That was the time when the shareholders had a right to be told what was happening, had a right to be consulted about the course this company should take in view of the difficulties with which it was confronted. If that is right, if there was a duty to tell the shareholder, he must be told plainly in words which will bring it home to his mind. As I said before, a phrase like "balance" instead of "profit," "adjustments of taxation reserves" instead of "taken from reserves" or "transfer from reserves" seems to me to argue an uneasy mind and a guilty conscience, and, as I said before, we are not here to attribute motive; but with regard to intention you must remember this, these two experienced business men knew every single thing that was going on. So far as Lord Kylsant is concerned, I have no doubt it may have entered his mind: "If I come out with the facts now, in the year 1927, I shall not be able to borrow any money for my new issue except on very onerous terms. If I can keep the flag flying for another year, I shall be able to borrow money on more favourable terms." That may have been in part the motive, but it is no excuse.

Members of the jury, in the performance of my duty, I have reluctantly to ask you to hold, first of all, that Lord Kylsant published these accounts, that they were false, that they were false to his knowledge, and that he published them with intent to deceive the shareholders; and with regard to Mr. Morland, that he aided and abetted Lord Kylsant in doing so. It is a grievous case, having regard to the honourable career of the two men in this Court, but, when all is said and done, far better than mere cleverness, we must keep our traditions scrupulously fair, upright, and our reputation for honourable dealing in the city of London untarnished if we are going to get out of the difficulties that confront us to-day.

Dealing now with the case that concerns the prospectus, you must

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remember that this is not a charge in which Mr. Morland is in any way implicated. It is a charge against Lord Kylsant, and Lord Kylsant only. I have already referred to the fact that in the years 1926 and 1927 there are letters recording the fact that Lord Kylsant was going to make a new issue. About June, 1928, Lord Kylsant sends for Mr. Lewis, who is an assistant accountant in the employ of the Royal Mail Steam Packet Company, Mr. Cason then being on his holidays, and Lord Kylsant says to Mr. Lewis: "What are the funds required for?" and Mr. Lewis answers: "Bank overdraft, losses from associated companies, and new buildings." Thereupon Lord Kylsant dictates a document to a clerk in Mr. Lewis's presence (Exhibit No. 41) which reads as follows:—

The audited accounts of the company show that during the past ten years the average profits (including profits of the insurance fund), after providing for depreciation and interest on debenture stocks, have been sufficient to pay the interest on the present issue more than — times over.

He tells Lewis to find out first of all the quantity of debenture stocks, and, secondly, how many times over could properly be filled in here. Lewis takes the document away and that very evening he leaves the answer at Lord Kylsant's house. I have not got the first print of the prospectus, but Exhibit No. 44 shows that the word "five" has been written in in the blank space. The final report of the prospectus is Exhibit No. 3. That prospectus shows the authorised capital, which was authorised by royal charter. It sets forth that the company was established in 1839 and that the object of the issue was to provide additional capital in the new freehold building, Royal Mail House, Leadenhall Street, and for the general purposes of the company. The company is said not to have issued debenture stock since November, 1914. The prospectus proceeds—

Although this company in common with other shipping companies has suffered from the depression in the shipping industry, the audited accounts of the company show that during the past ten years the average annual balance available (including profits of the insurance fund), after providing for depreciation and interest on existing debenture stock, has been sufficient to pay the interest on the present issue more than five times over.

As the interest on the present issue, which is an issue of £2,000,000, would be £100,000, more than five times over is a way of saying more than £500,000; and observe the heavy leaded type; "sufficient to pay the interest on the present issue more than five times over."

Now, let me make this observation to you about that document. I am not for a moment going to consider detailed words and phrases. Think of the type of person to whom this was addressed. It was addressed to the prospective investor, and presumably the prospective investor of a more or less cautious type. This is not anything like a gamble. This is almost gilt-edged stock. See how this document strikes him and must have been intended to strike him. What is the relevance of setting out the past at all? Why say what you were doing in the past? Why say

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that you have been earning—and saying it in leaded type—more than £500,000 a year, unless it is that you obviously mean anybody to draw this conclusion: “From what has taken place in the past you may legitimately draw an inference as to what will take place in the future.” It is quite obvious to every one of us that that is the object. Now, could you possibly on the facts of this case, as you know them, draw any inference as regards the future, from the fact that during these years these sums of money had been expended in dividend? Is it not utterly dishonest—and I do not mince my words—to put a document before a prospective investor and say to him: “Now, this is what we have done in the past,” and imply to him: “What we have done in the past is a fair indication of what you may reasonably expect we shall do in the future.”

There are two other points to be discussed about this document. What do the words “average annual balance available (including profits of the insurance fund)” mean? What was the ordinary investor intended to understand by that? Take one year as an illustration. Let us take the year 1924. Are you not saying this: “In the year 1924, after providing for all taxation, after providing for depreciation of the fleet, after adding to the reserves, after payment of dividends on preference stocks, the dividend in 1924 was 6 per cent.”? In my submission that is all it can be. See how carefully those words were selected. In truth and in fact in the year 1911 this company was not very prosperous, and therefore, for aught I know—and I believe it to be the fact—it had practically no reserve at all. Then comes the war, and with it this great prosperity, and it is building up its large reserve funds. Then comes the period after the war, and you start rapidly living on the reserves which you have made in the war. Is not the sense in which these words are used quite plain? Suppose this company had at this time gone to the City and asked the investor to invest money, stating what had taken place within the last seven years, is there any one single man, woman, or child who would have lent money? You know, and everybody in this Court knows, that the answer to that is “No.” It is so fatally easy for a clever man in a big position to select phrases which will conceal the truth and perhaps at the same time enable him to say: “Oh, well, look at the words which I used; consider them carefully. Put your finger on any statement that is positively untrue—particularise it.” You must look at this document as a whole and treat it as a whole. “Although this company in common with other shipping companies has suffered from depression in the shipping industry,” see what that phrase means. What it is saying is this: “Bad times though we have been having, yet we have been able to pay on an average £500,000 a year.” What is the relevance of saying that unless you mean that you are paying it out of your current earnings? There is no relevance in it at all if you are paying it out of past profits. The whole thing, in my submission to you, is that it is a deliberate statement, very carefully phrased, and very cunningly devised. As Lord Kylsant, I regret to say, thought

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it proper under his influence and with his authority to put this document forward, it must have been intended to deceive unfortunate people up and down the country to put their money into this concern which, unless something radically different happened very soon, would certainly slowly but inevitably drift on to the rocks. There again the question for you is: was this document a false document in the sense which I have described? Was it known to be false, and was there an intention to deceive? Members of the jury, I suggest to you it is quite obvious that there was an intention to deceive. If so, your duty is to return in that case a verdict accordingly.

I have finished opening, but there is just one other matter I should like to refer to, and that is the way this matter came to light. There had been some money advanced in connection with the trade facilities, and Lord Plender, a very eminent and distinguished man, who assists the Government and advises the Government in regard to their trade facilities, took the view in October, 1929, that as there was a question of further time being required it was desirable that the Government should have the whole matter looked into by some accountant who had no connection whatever with it, and he relied upon Sir William M'Lintock to look into the matter to see whether the extension of a guarantee should be granted by the Government. That is all Lord Plender knows about it, but I understand my learned friends desire that Lord Plender should be called. I shall call Lord Plender for that purpose, and before I sit down I want to say this word about Sir William M'Lintock. Sir William M'Lintock came upon the scene and was requested by Lord Plender to report in connection with this company, and accordingly he made a report and set out to the best of his ability what he found to be the case. I have no doubt that Sir William M'Lintock is in a more invidious position than any one has ever been placed in. I hear some one say "Why?" I should have thought the answer was quite obvious. Can any one imagine a more invidious position than having to go into the witness-box to give evidence in a case in which a distinguished member of your own profession is concerned? But he comes here—and I want this to be plainly understood—in answer to my *subpoena*. I am responsible for the conduct of criminal proceedings in these Courts and Sir William M'Lintock is not. I do not propose to ask Sir William M'Lintock any questions except such questions as are contained in the report which he made in answer to the instructions which Lord Plender gave him. If my friends choose to ask him about other matters, they are perfectly entitled to do so; but it is only fair to him to let you understand from me that, having made this report, the rest of the responsibility is mine, and I am going to take it and not shelter behind anybody else or allow anybody else to concern themselves in matters which are my province.

Sir PATRICK HASTINGS—Before your lordship adjourns, may I renew my application which I made this morning? Your lordship will appreciate there has been a considerable change since this morning,



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in that by this time the Attorney-General has dealt fully with the two branches of the case which he had to open, and I do most respectfully ask your lordship to say that now, having heard the opening, the prosecution are not entitled to put the whole of these charges into one indictment, and that they should be dealt with separately.

Mr JUSTICE WRIGHT—Well, Mr Attorney-General, do you desire to proceed with the case as a whole?

The ATTORNEY-GENERAL—I do.

Mr. JUSTICE WRIGHT—If that is the Attorney-General's desire, I think he is entitled to do it.

The Court adjourned.

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Second Day—Tuesday, 21st July, 1931.

## Evidence for the Prosecution.

Lord PLENDER, examined by the ATTORNEY-GENERAL—I am senior partner of the firm of Deloitte, Plender, Griffiths & Co., chartered accountants. I have been president of the Institute of Chartered Accountants on several occasions, and have served on a great number of Royal Commissions and Government Committees. I was a member of the Trades Facilities Act Advisory Committee, which was constituted in 1921, and I became its chairman in 1925. The object of the Committee was to assist companies to raise money on advantageous terms with Government securities, and the Committee were to advise the Treasury on the applications which were received. The Trade Facilities Act came to an end in March, 1927, and from that date no new guarantees were given. There were still, of course, the existing guarantees which had to be dealt with; the members of the Committee were asked to continue to advise the Treasury when called upon, and I personally was consulted from time to time by the Treasury with regard to the existing guarantees. In October, 1929, an application was made by the Royal Mail Steam Packet Company with regard to their existing guarantees, and Lord Kysant came to see me with regard to the postponement of certain claims.

Were they loans due for repayment at the end of 1929 and in 1930?—Yes. Towards the end of 1929 certain statements were supplied to me by Price, Waterhouse & Co. Certain reports were received, and after consultation with the Treasury the conclusion was come to that the Treasury had not the facilities to examine the reports in detail, and it was suggested that it would be advisable to have some independent person to look into the matter. Price, Waterhouse & Co. had been instructed by Lord Kysant to make the report, and when Sir William M'Lintock was instructed to make a report there was certainly no reflection at all on Price, Waterhouse & Co.

You were bringing a fresh accountant to examine the whole thing?—We wanted some one to make a report who had no connection with the companies. Several names of well-known chartered accountants were discussed, but it was decided to select Sir William M'Lintock to make the investigation.

Was Lord Kysant informed that Sir William M'Lintock had been nominated for the purpose?—Yes, he was informed in December, 1929. He immediately said that every possible facility should be given to him, and Sir William M'Lintock stipulated that he should have a free hand.

And did he have a free hand?—I believe that every possible facility was afforded to him. I have never seen the books of the company, I have

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never seen the officials of the company, and I know nothing of their explanations.

And really all you can tell us is how Sir William M'Lintock came upon the scene?—Yes, I understood from the Treasury that that was why I was called here, to narrate the facts leading up to his appointment.

Cross-examined by Sir PATRICK HASTINGS—I have known Mr. Morland for many years. I never had any professional dealings with Mr. Morland, but I came into close contact with him when I sat on the Trade Facilities Act Committee.

Do you know any member of your profession who enjoys a higher reputation for absolute honesty and integrity than Mr. Morland?—I do not.

I understand from the question which the Attorney-General has put to you that you have not had any opportunity of looking into the figures of this company, and that you know nothing about them?—No.

Sir PATRICK HASTINGS—I desire to ask some questions with regard to what the Attorney-General has referred to as “secret reserves.” I would like to refer to them as inner reserves.

Mr JUSTICE WRIGHT—Why the difference? I have seen them called internal reserves.

Sir PATRICK HASTINGS—It sounds rather better.

Mr. JUSTICE WRIGHT—What difference does it really make?

Sir PATRICK HASTINGS—Whatever we call them, it is a practice of many of the large commercial enterprises in the country to have inner reserves.

The WITNESS—It is quite usual for large commercial and industrial companies to set aside out of an unusually prosperous year sums to secret reserves.

*Cross-examination continued*—Is it quite a usual and proper thing for companies to set aside large sums against their liability for excess profits duty?—That is the case when a company knows that a liability will mature some day, and as prudent people they would make provision to meet that liability when it matured.

And in the ordinary case, such a reserve would be set aside out of the profits for the year?—Yes.

In such a case, when it was discovered that they were not required, they would properly be brought back into the profits for subsequent years, and exactly similar conditions would arise in the case of reserve for income tax?—Certainly.

In the Attorney-General's view, up to a point those secret reserves being brought back in many cases would not be disclosed in a profit and loss account as having been brought from secret reserves?—Sometimes no reference is made, but sometimes there is an indication that some transfer was made.

Do you agree that secret reserves are used for that purpose, and there sometimes comes a time when an auditor should say that some indication should be given to the shareholders that those transfers

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were being made?—Yes, I have known of cases where there was no longer a requirement to keep a reserve for excess profits duty, and it was brought into the credit of the profit and loss and no mention was made that reserves had been called upon at all.

This is done by firms of the very highest repute?—Yes

Do you agree that there may come a time when the auditor may say that if the reserves are to be used again some indication must be given to the shareholders that the profit and loss account has been augmented by transfers from the excess profits duty or other reserves?—Yes.

And supposing the auditor comes to the conclusion that it is right and proper that some indication should be given of that fact, are there some very well-known phrases which are commonly used by auditors to indicate it?

Mr JUSTICE WRIGHT—Well-known to whom?

Sir PATRICK HASTINGS—To the auditors. (*To Witness*)—Is it usual among accountants to employ various phrases such as “taxation adjustment” and “after adjustment for income tax reserve not required”?—That is so.

Do you agree that those transfers might be either small or large?—Yes.

If you saw such words you would understand that there had been transfers from excess profits duty or otherwise which might be small or large?—Certainly.

By the COURT—How would you translate the word “adjustment”?—The definition I would give is this: the difference between the sum or sums, reserved or set aside, to meet maturing obligations whose precise ascertainment is not known at the time such provisions are being made, and the amount of the actual liability when it is ascertained and settled.

*Cross-examination continued*—In using these words in the profit and loss account, “adjustment of taxation reserve,” these are words not uncommonly used by accountants?—I have already said so.

Would you agree that some shareholders would never understand a balance sheet at all? They would not know, perhaps, the difference between the words “credit” and “debit”?—It is very difficult to know the minds of other people.

Of course, if you give an indication to shareholders of the facts you have mentioned, the balance sheet and profit and loss account are sent out to shareholders before the annual general meeting?—Yes.

Do you agree that any shareholder who wants to know how much has been transferred, or any other question regarding the accounts, or regarding anything, is perfectly at liberty to ask for the information at the meeting of the company. Assuming that there is no amount specified, it is quite open to a shareholder to ask for information?—Certainly. I can conceive of cases in the commercial world in which it is properly unwise for directors to give to the world indications of how their business is progressing. If a shareholder liked to ask

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questions, then the chairman at the meeting could give to the shareholder such further information as he thought it was proper to give. The auditor, of course, would have no control over the questions which were to be asked by the shareholder or the replies which the chairman might give. In addition to what has been referred to as hidden reserve, a great many companies have in addition a published reserve, and the published reserve appears in the balance sheet every year.

And if any sum is taken from the published reserve for the credit of the profit and loss account, that appears as a mathematical calculation from last year's balance sheet?—Yes.

In practice an auditor is bound to be influenced by, and pay a great deal of attention to, the honesty and ability of the composition of the board for whom he is working?—Yes.

Was not the board of this company a very distinguished one?

Mr JUSTICE WRIGHT—Is it desirable to go into this?

*Cross-examination continued*—Do you recognise one member of the board who is one of the most distinguished lawyers practising to-day?—Yes.

I want you to assume that never in his life has Mr. Morland ever owned, bought, or sold a single share in any of these companies. Is there anything contrary to the practice for an auditor to buy and sell shares in the company in which he is auditor?—I think that an auditor does occasionally have shares in companies which he audits.

Mr. JUSTICE WRIGHT—Why go into this?

Sir PATRICK HASTINGS—I had a reason.

Mr. JUSTICE WRIGHT—It might be very wrong for an auditor who had access to the inner workings of the company to buy or sell shares.

*Cross-examination continued*—Are the accounts generally passed by the board before they come to the auditors?—That is rather a difficult question for me to answer. My experience is that when an audit has taken place in a big company the examination may take many weeks, and the auditor has to proceed with the work before the directors hold their meeting. I appreciate the fact that the clerical work is very often done, not by the partners in the firm, but by a clerk. It is not in every case that the accounts go then before the board. In some cases, perhaps, the auditor would not see the accounts until they were passed, and in other cases he would. I do not think there is any general practice.

By the COURT—Can it affect the accountant in any way or not?—I don't think so. The accounts are the accounts of the directors, and the auditor's duty is to examine and report on them.

Sir WILLIAM M'LINTOCK, examined by Mr. PRITT—I am a chartered accountant, and the head of the firm of Thomson M'Lintock & Co. I investigated the affairs of the group of companies known as the Royal Mail Steam Packet group. I was given every facility in my examination. The chairman and managing director of the company is the defendant, Lord Kilsant. With regard to the position in 1926 and

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1927 of the 100 per cent. subsidiary companies, in 1926 the R M S P. Meat Transports, Ltd, showed a trading loss of £21,945 after charging depreciation.

And in 1927, after charging depreciation, the trading profit was £28,657?—Yes.

Did the company bring in transfers from old reserves in each year—in 1926 £62,500 and in 1927 £25,250?—Yes.

Did it declare dividends payable to the R.M.S.P. in each of those years?—Yes.

Did they absorb net £49,000 each year?—Yes. I dealt with the two Nelson companies together. The actual working position was that H. & W. Nelson, Ltd, was the company which managed the other concern. Those two companies made profits in both years, after charging depreciation—in 1926, £80,229 and, in 1927, £38,113.

By the Court—Were there any debentures in these companies?—There were debentures in the Navigation Company; I don't know if they existed at that time.

*Examination continued*—In 1927 the Nelson Steam Navigation Company declared a bonus of £200,000, and H & W Nelson, Ltd, a bonus of £100,000. There were transfers from the reserves of those two companies in 1927 of £185,859. The two bonuses were credited in the accounts of the R M S P. in the profit and loss account for the year to December, 1927. The bonuses were actually declared in December, 1927, and cheques in payment were issued by the two companies to the R.M.S.P., which was the shareholder concerned. The cheques in favour of the R M S P. were for the sum of £300,000.

During that month did the R M S P. apply for a further 1,000,000 £1 shares in the Nelson Steam Navigation Company?—Yes.

Did they pay for half of those shares in full?—Yes.

That is to say, £500,000?—Yes.

And issue a cheque for that sum?—Yes, I understand so.

Did they also pay out 2s. per share on the other half a million shares and issue a cheque for £50,000?—Yes.

Now, as far as we have got, the two Nelson companies handed the R.M.S.P. cheques for £300,000, and the R.M.S.P., in its turn, issued to one of the companies cheques for £550,000?—Yes.

In the same month of December, did the R.M.S.P. also sell to the Nelson Steam Navigation Company the whole of the share capital which it held of H. & W. Nelson, Ltd., for £250,000?—Yes.

And thus the various cheques issued by and to the R.M.S.P. were £550,000 in, and £550,000 out?—Yes.

Leaving the actual cash position as it was before?—Yes.

When the operation was over, the R.M.S.P. held the whole of the shares in one of the Nelson companies, and that Nelson company held the whole of the shares in the other Nelson company?—Yes, the result was just the same. The whole of the operations referred to took place in the latter part of December, 1927.

In order to arrive at a proper result of David M'Iver & Co.'s

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trading, I took the view that I should make some alteration in the charge for annual depreciation. In that connection I adopted a systematic method all through with all the companies when calculating depreciation. On the basis on which I calculated depreciation, there was a modest increase in the case of M'Iver & Co. The company's accounts in 1926 showed a loss of £5158, and my view was that the loss should be £4563. To the latter figure I added a transfer from income tax reserve of £16,273, which showed an adjusted loss of £20,836. The adjustment of the depreciation represented an amount of £10,255. That made a total adjusted loss of £31,091. The company did not pay any dividend in 1926. In the following year I again calculated the depreciation on the same basis, and that involved an increase in the depreciation allowance from £12,000 to £18,965. On the face of the company's accounts there was a profit for the year of £855. I increased that figure by £5000, but deducted the sale of investments. A profit was left, but after deducting certain other items and adding the increased depreciation the adjusted loss for the year was £28,200. Again, in that year, the company did not pay any dividend.

The next company is the larger company, the Pacific Steam Navigation Company. I produce a copy of that company's accounts for the year 1926, which show a profit, after charging depreciation, of £60,532. That sum is arrived at by taking the "balance available" of £80,858 and deducting £20,326 brought forward from 1925. The net figure of profit for the year is £60,532. I estimate that the actual trading loss for the year, after charging depreciation on the usual basis, was £183,755. The difference between that £60,532 and £183,755 is £244,287.

How was that figure made up?—Profit from the sale of vessels, £11,241; transferred from obsolescence account, £148,000; and a transfer of what we described as "Sundry credit balance not required." Those three items make a total of £244,287.

Do any of those items fall within the classification of reserves?—I suppose the obsolescence account might be considered a reserve, and the £85,000 credit balances, against which there was no liability, would become a reserve.

In that year a dividend was actually declared and paid to the Royal Mail Steam Packet Company which absorbed £60,000?—Yes.

The report of the company for the year 1927 is drawn up in substantially the same form as that for 1926. The profit for the year is almost the same, the actual sum being £59,422. My view is that in fact there was a loss on the year's trading of £160,748. The difference between the two figures is £220,170.

How was that made up?—Profit on the sale of vessels, £28,070; transfer from obsolescence account, £75,994; transferred from miscellaneous reserves, £32,433; surplus of income tax reserve, £48,246; and sundry credit balances not required, £35,427. That makes a total of £60,000.

So far as the subsidiary company, MacAndrews & Co., Ltd., is

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concerned, I have calculated the depreciation on a twenty years' life basis. In 1926 the depreciation allowed was £75,000, and my own calculation is within a few pounds of that amount. In 1927 the company's provision was £19,778. I, however, calculate that the provision should have been £76,058. The company's accounts showed for 1926 a loss of £52,973. My calculations involve a certain number of adjustments, but they are small. My figure for the adjusted loss for the year is £57,107. In that year no dividend was paid. In 1927 the company's accounts showed a profit of £9778. I made one or two minor deductions, and the main difference was in regard to depreciation, which was as much as £50,000. The adjusted loss for the year, according to my figures, was £17,428. No dividend was paid by the company in that year.

Summarising the results of the figures you have gone into for the six 100 per cent. subsidiaries, do you calculate that 1926 showed a loss on the six companies of £213,669?—Yes.

And 1927 showed a loss on the six companies of £169,606?—Yes. In 1926 certain of the companies declared either dividends or bonuses amounting to £151,000, while in the following year the amount was £425,000. The R.M.S.P. had, of course, interests in concerns other than the 100 per cent. subsidiaries, which brought in dividends.

Referring now to the accounts of the Royal Mail Steam Packet Company itself, on the company's figures for 1926, the balance to the credit of the profit and loss account, after charging debenture interest and depreciation, was £355,325. That was the published profit for the year. The balance for the year was £439,000. There were rents of properties amounting to £38,000, transfer fees £416, and a sum of £150,000, which was described as "transfer from reserve funds." The total of those items was £628,000. To arrive at the profit for the year, it is necessary to deduct the First Debenture interest of £63,000, £155,000 for the 5 per cent. debenture interest, and discounts and interest of £55,209. After those amounts have been deducted there is a profit for the year of the amount already mentioned of £355,325.

On the face of the accounts there is the figure of £355,325; in arriving at that figure, were transfers made from various unpublished reserves?—Yes.

Were they £175,000 from the income tax reserve?—Yes.

And £550,000 from the E.P.D. reserve?—Yes.

The other is the transfer of £150,000 appearing on the face of the accounts?—Yes.

Those first two figures of reserves—have they at any time, as far as you can ascertain, been disclosed on any published documents of the company?—No.

Was there in 1926 or in 1927 any disclosure of there being transfers from reserves to the profit and loss account except anything we may see on the face of the printed document?—No.

Was a substantial amount of those reserves free from any period prior to the end of 1926?—Yes, it was known that there was a very large sum free about the end of 1923.



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By the COURT—The liability in respect of excess profits duty has been practically ascertained?—The accounting period in that respect ended in 1921.

Sir JOHN SIMON—I would like the evidence of the witness on that particular matter to be given in rather more specific form.

By the COURT—You have been dealing with the R.M.S.P. Company's reserves from excess profits duty. At the end of 1923 it was known that a certain amount would be excessive?—The provision which had been made by the company was in excess of the probable liability. Certain of my information was obtained from the assistant accountant in the R.M.S.P., who dealt with taxation matters. I was also shown a letter —.

Sir PATRICK HASTINGS—I object to any such evidence being given.

By the COURT—The evidence is objected to on the ground that it is only known as hearsay. Can you give any information of your own knowledge? Of course, the books of the company are in Court. If information is only to be given from actual knowledge, there will be considerable difficulty experienced with regard to accountancy evidence. You have said that the provision was excessive. When did it become finally known that such was the case?—I think it was some time in 1926 or in 1927. Before that it was well known —.

Sir PATRICK HASTINGS—I do not think Sir William can say this.

Mr. JUSTICE WRIGHT—When a Court is dealing with accounts, it is impossible to apply the strict rules of evidence, such as when evidence is given by an eye-witness.

Sir JOHN SIMON—The witness has said that something was "well known," and I am anxious to ascertain if there is any document which could be produced on that point.

*Examination continued*—In arriving at the true position of the Royal Mail Steam Packet Company for 1926, I took into account the insurance items. The company charged in every voyage account a regular figure, calculated on a proper and reasonable basis for insurance. Those sums, in the course of accounting, were all credited to the insurance fund, which was not unnaturally drawn upon for the expenses of insurance. That insurance fell into two classes. When insurance was effected with the outside underwriters, the fund was used to pay the premium, and in the second place the company naturally underwrote some portion of the risk. The company underwrote a small portion of their own risk, and the claims arising under that were charged to the fund. The whole purpose of that portion of my report was that I was asked to report on the current earnings, and my report was directed to that alone.

It was particularly important that you should arrive, item by item, at a perfectly accurate view?—Yes, I had to deal with items on both sides of the account.

With regard to the insurance fund, you considered that the company should be legitimately credited with a sum of profit which it had not in its own books credited to itself, and the figure was £44,404?—Yes. In arriving at what I regard as an accurate view of the year 1926 trading

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of the R M S.P. Company, one ought to deduct the £14,101 from the £875,000, which I regard as not earned in the year, and that shows a net figure of £830,596. There was also a profit on the sale of vessels of £6093. Those vessels had been written down below what was obtained for them. There was also a profit on the sale of investments of £25,770. If those two figures are added to the net figure you get a total of £862,465, which might be described as composed of items which, in my view, do not relate to the trading operations of the year.

Of that £862,000, £150,000 does appear in the profit and loss account, and the balance sheet?—Yes.

But in the profit and loss account and the balance sheet none of the others appear?—No.

We started with your figure of £355,000 as the profit shown for the year on the face of the accounts. If that is compared with your total of £862,000, does it show that in your view the year 1926 showed a trading loss of £507,140?—Yes.

After charging debenture interest and depreciation?—Yes.

There is one other figure which, in your view, it is fair to take into account. Calculating depreciation on the uniform basis you have always applied, if you compare your figure for 1926 with the company's figure, you find that the company had actually charged a larger figure for depreciation of between £60,000 and £70,000?—Yes.

Is your calculation £553,581, and the company's actual charge £620,747?—Yes.

If that difference be credited against the £507,140, which you tell us was the trading loss for the year, it would make the loss for the year on the trading results of the company £439,994?—Yes. In the figure I have included the dividends received from all allied and other companies. The 100 per cent. subsidiaries contributed dividends in that year of £151,000. With regard to the accounts of the R.M.S.P. for 1927, in that year there was no transfer from the published reserves. The total of the three items on the credit side of the profit and loss accounts was £737,000, and, deducting the charges for debenture interest, &c., there was a "shown profit" for the year of £489,880, as compared with £355,000 in the preceding twelve months.

Did the company take sums of money from three reserves totalling £385,693?—Yes.

Income tax reserve, £120,000; E.P.D. reserve, £232,780; and corporation profits tax reserve, £32,905?—Yes.

By the Court—What did you think was the position in 1927 in regard to the excess profits duty and the income tax reserves?—There was a sum appearing in the books of the company to the credit of the income tax account. There was transferred from it to the profit and loss account a sum of £120,000. I was not particularly concerned in reporting on that matter, except as to whether the £120,000 related to the year 1927. I excluded it from the earnings of that year because it did not relate to it.

As far as you were concerned, you were reporting on the earnings

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of the company?—The current earnings The transfer from the excess profits duty of £232,780 was the last that was made The sum that was standing to the credit of that account in the books was exhausted. It was closed by the transfer of £232,780. The corporation profits tax reserve I knew did not relate to 1927. I did not make any detailed investigation on the point. There was no need for it so long as I was satisfied that the item did not relate to the particular year If I had any questions to ask, I put them to the officials in the company's offices, and they most readily gave me all the information I sought in order to enable me to come to a conclusion as to whether items related to one year or another.

*Examination continued*—With regard to 1927, so far as you have been able to ascertain, has the existence of any of these free reserves ever been disclosed in any public document?—The figures, no, but there are the words in the profit and loss account, "Adjustment of taxation"

By the COURT—The amounts have never been disclosed in any form or any published report or accounts?—No.

*Examination continued*—In 1927 the surplus from the insurance fund was £10,808. However much the balance was at the end of the year, the company never treated it as a profit in 1926 or 1927. In the latter year there were items relating to profits on the sale of vessels and the sale of premises The profit on the sale of vessels was £18,593, and on the sale of premises £90,338 In my view, all those figures, totalling £483,816, are not part of the profits earned during the year. The amount shown in the company's accounts was £489,880, and, deducting the £483,816,\* that left a balance of £6064, which for the moment might be termed the profit for the year.

When we come to the depreciation, I think the company is charged £493,034, and the figure which you have taken, calculated on the usual twenty years' basis, is £524,861, or a difference of about £41,000?—Yes.

If that is marshalled with the £6064, it shows for the moment a loss for the year on balance of £35,753?—Yes.

In the figures is included the dividends and bonuses received from the 100 per cent. subsidiary companies of £425,000?—Yes.

Of which £125,000 is in dividends and £300,000 was the two Nelson bonuses?—Yes.

With regard to the accounts of the R.M.S.P. and its six 100 per cent. subsidiaries, what do you estimate the trading losses were for 1926 after charging debenture interest, interest on loans, and depreciation?—£804,663. The net actual distribution to the shareholders, &c., of the company in 1926 was £346,800, and in 1927 it amounted to £386,800. The difference of £40,000 was due to the fact that in 1926 the dividend paid to the ordinary shareholders was less than that declared in 1927.

Cross-examined by Sir JOHN SIMON—Do business people and accountants recognise the distinction between a trading account and a profit and loss appropriation account?—Yes, they do.

\* As stated in an earlier answer £385,693 was transferred from reserve.

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It is a perfectly well understood distinction. A trading account of a business company in any year would be a statement of the earnings of the company from its trading on the one side and what it had cost the company to make those earnings on the other side?—Yes.

The difference between those two would give you a balance either on one side or the other, which would be either a trading profit or a trading loss?—Yes.

Is that all perfectly familiar in business and in accountancy?—Perfectly.

Do I really understand that in such an account as that you would not bring in such things as dividends from investments?—No; the term "trading and profit and loss account" is sometimes used a bit loosely, as distinct from profit and loss appropriation account. It is usual to put the trading items first and then such other things as dividends from investments. It is not usual to publish details of the trading items, showing the expenses, except in total. In a trading account you would not get brought in such things as returns from the company's investments. It would be limited to the trading.

By the Court—It ought to be limited to the earnings on the trading of the company, as if it had no external investments?—Yes.

*Cross-examination continued*—Look at that copy of the accounts of the Royal Mail Steam Packet Company for 1926. The profit and loss account states that it includes dividends on shares in allied and other companies. There also appears a reference to the rents of properties and other matters. Any competent business man or accountant, looking at the document, would know at once that it was not a trading account, but a profit and loss appropriation account?—No, it is not a trading account, but it is not a profit and loss appropriation account.

Any competent business man and any competent accountant, as soon as he sees that document, knows it is not and does not purport to be a trading account?—No, it is only an account intended to show the result of the trading, plus the other things shown there.

What you have been doing in some of your answers was recasting or re-forming this page of the accounts so that it would become a trading account?—No.

I thought you were endeavouring to ascertain for the year 1927 whether there would be a trading profit or a trading loss?—I was.

You have this morning been telling the jury what you regard as the trading result of the year 1926?—The trading result, having regard also to dividends. I left in my totals, for example, the dividends which the Royal Mail had received from other than the 100 per cent. subsidiaries. I did not exclude them.

By the Court—You did arrive at what you considered to be the trading result?—Including those dividends, yes.

*Cross-examination continued*—I understand you have been working out figures which to your mind show a trading deficit for the year?—That is so.

By the Court—Is there anything to indicate whether the trading



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operations of the company for the year resulted in a profit or a loss?—No, it does not indicate it.

There is nothing to indicate whether the trading operations resulted in a profit or a loss?—That is not unusual

*Cross-examination continued*—It might be that the document would not give the information one way or the other?—No, it does not.

Referring to the depreciation which you have allowed in arriving at your own figures regarding the trading of the R.M.S.P., you have referred to the "usual depreciation"?—I said that I had adopted a definite method throughout all the groups. It must be remembered that I was dealing with twelve different groups, and the Royal Mail is only one. The method I followed was to make a calculation on the basis of the twenty years' life. I made no charge in the case of vessels which had been reduced to scrap value, and I followed that method throughout all the Royal Mail group and all the groups with which I dealt.

Is it your view that the twenty years' life, which is a 5 per cent. basis, is the usual one?—It is a very common basis

Is there any usual basis for the depreciation of vessels?—I only know of one that could be termed "definitely the usual basis," and that is the Inland Revenue basis, which is 4 per cent.

The only usual basis you know is that of the Inland Revenue, which is 4 per cent. I think you served on the Royal Commission on Income Tax?—Yes.

One of the things which the Royal Commission on Income Tax considered was the difficult subject of the proper allowance for depreciation in connection with income tax?—That is so.

Do you remember the evidence given on behalf of the Revenue on the subject of the depreciation of ships?—I do not. If it is assumed that a ship has a twenty years' life, then the depreciation would be at the rate of 5 per cent. on the initial cost. On the other hand, if the life of the vessel is estimated at twenty-five years, the depreciation would be at the rate of 4 per cent.

Would not 5 per cent. be an unusual amount to write off, in the sense that it is setting aside more than might be regarded as quite sufficient?—More than the normal. There might be circumstances which would make it proper to write off more, having regard to the type of vessel, and the cost at the time of building.

Is there anything known to you in the records of the Royal Mail Steam Packet Company which makes you suggest that in the present case 5 per cent. is necessary and 4 per cent. is too little?—The answer is neither "yes" nor "no." It was perfectly well known to me that the ships were built when costs were high. I do not pretend to a detailed and accurate knowledge of every ship the R.M.S.P. possesses. I examined the costs of all the vessels, and their ages, and adopted the twenty-year life basis as being what I thought was a fair one.

In more than one case, when ships came to be sold, they were disposed of for more than the value that existed in the books?—Yes.

Other things being equal, is that an indication to a candid mind

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that it may be that they write down the ships too severely?—I agree, wherever the price realised is in excess of the book value it is an indication that the depreciation may have been too high.

Are you aware that, apart altogether from this 5 per cent. depreciation, there was a sum of £1,152,000 set aside by Lord Kylsant and his directors as a special reserve for depreciation?—There was a sum. I know the details of the account; I have not them in my mind.

Was this £1,152,000 over and above the 5 per cent.?—I have already explained I have not investigated the earlier years, when it was built up, but I think it might be taken quite definitely that it was over and above.

It comes to this, that when you take the accounts of the company, and make such adjustments as you think proper, you have not made any allowance at all, have you, for the fact that there was this special depreciation reserve of over one million sterling?—No. I think it is only right to say I made a complete report, and in that report I set out all that I have done, and how I arrived at my figures. There is only before the Court a small portion of that report.

In your report you arrive at a value of the fleet on a twenty-year life basis?—Yes.

What was the total of the value so arrived at?—The total of the twenty-year life of the combined fleet was £15,212,598.

Did you at the same time ascertain at what figure the fleet stood in the books?—Yes, £13,500,000.

You knew that the fleet had been written down in the books by one and a half million sterling below what it would be valued at even on a 5 per cent. basis?—Even on the twenty-year life basis, yes.

Supposing you substitute a 4 per cent. basis, could you tell us roughly what the difference would be?—It would make my £15,000,000 bigger, of course, and it would make the contrast between that and the book value still larger.

Referring to income tax credits and E.P.D. reserves, I understand that the sum of £175,000 was transferred to profit and loss account in 1926. Is it your view that that sum was an old reserve?—It is not my view, and my reason for putting it in my statement was that it did not relate to the year 1926.

In order to trace the origin of this amount, I refer you to a summary of the income tax ledger, and to three items totalling £196,000 odd. The first of these is a figure of £121,237, representing tax deducted from dividends paid; a figure of £5190 cash; and a figure of £70,000 representing repayment of tax on E.P.D. There is a deduction of £13,960 from this figure, leaving a balance of approximately £180,000, and my suggestion is that that £180,000 had arisen in the year 1926?—With regard to the tax deducted from dividends paid (£121,237), I would point out that it is the proportionate deduction which the company was entitled to make when it paid the dividend, and nothing is more clear than that the company, when it did deduct such an amount, did not deduct it as an agent of the Government, but

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kept it. So that in the course of the year 1926 the company had got that amount and had not got it at the commencement of the year

Do you agree that the company got it by deduction?—Yes.

Coming to the amount of £70,000, do you admit that this amount was received during the year 1926?—Yes.

Am I not right that each of these figures, whether plus or minus, arose within the year 1926?—These figures do, undoubtedly

The amount is just over £175,000?—That is so

Then it is the case, is it not, that £175,000 and a little more was a credit in the income tax reserve account and £175,000 was transferred in the year 1926 to profit and loss?—Yes, that is so.

In the profit and loss account for 1927 there is a figure of £697,456, one item of which is in respect of income tax, £120,000. That had arisen in a corresponding manner to the figure mentioned in regard to 1926?—Yes.

I agree that the income tax account was built up in the same way in both years, except that there was a large charge for a sum allowed from subsidiary companies in one year, and I do not know how that affected it.

Is it correct that in the course of 1926 the company received from the Revenue rather more than £175,000 on income tax account, and that in the course of the year 1927 the company received rather more than £120,000?—That is so.

Then it would appear that the £175,000 in the year 1926 and the £120,000 in the year 1927 were, as a matter of fact, transferred to profit and loss account in the years in which they were received?—That is so

Assuming that these amounts fall into the hands of the company, they are amounts of a sort and character and kind which is distributable in dividends. They form, that is to say, a portion of the credit which goes into the profit and loss account?—Yes, the tax retained in effect makes the payment of the debenture interest less and provides a fund out of which dividends could be paid if you account to the Revenue for them.

If I compare the situation in that income tax account at the beginning of the year 1926 with the situation at the end of the year, would it be correct to say that Lord Kysant and the accountant were drawing money out or putting money in?—The balance was greater at the end of 1926 than at the beginning.

So that the reserve, so far as that account was concerned in 1926, was increased?—Yes.

With regard to excess profits duty, is the same thing true in respect of the transfers from E.P.D. account to profit and loss account for the years 1926 and 1927?—The composition of the two accounts differs. They had started building up the E.P.D. account year by year from the time the tax was imposed, *i.e.*, 1914.

I suppose you would agree that it would be a prudent thing for a company not to transfer sums from E.P.D. account to profit and loss account until they knew they were safe?—That is why I assume they started in 1922.



# The Royal Mail Case.

Sir William M'Lintock

Referring to the allowance made to the company by the Revenue in respect of obsolescence, the great British shipping companies were appealed to to build, and did build, all the shipping they could during the most difficult days of the war, often at very high prices, to replace the tonnage that was being sunk. Consequently, the Government promised that they would in some way make it up to the shipping companies who had built the ships when prices were very high, by allowing them an allowance in respect of obsolescence. Did the settlement of this matter in the case of the R.M.S.P. involve years of discussion?—Yes, and I was told that the obsolescence allowance was settled in 1923.

I put it to you that it was actually settled in 1927?—I believe a very large proportion of the claim was admitted in 1923.

With regard to the deferred repairs allowance, can you say in what year the R.M.S.P. settled this matter with the Government?—I do not know.

Was it about 1926?—The final settlement might have been then.

I refer you to a letter, dated 22nd April, 1921, from which it appears that there was an agreement, for the year 1917, that £546,198 would be the agreed charge on E.P.D. against the whole Royal Mail group. That letter is from a firm of chartered accountants in Liverpool, and states that the computation of duty for 1917 had been agreed with the Inspector of Taxes, and that the amount of the assessment was £546,198, in respect of which £545,875 had been paid on account?—Yes.

By the Court—What is meant by the expression “Royal Mail group”?—It refers to the R.M.S.P. Company itself and its 100 per cent. subsidiaries.

*Cross-examination continued*—If the £546,198 was settled finally in respect of the group, the R.M.S.P. itself would only get its portion of that. Do you know that in 1927 the Revenue, so far from agreeing the figure of £546,198, finally agreed a figure of £976,048?—No.

Do you know that of the £976,048, the proportion of the R.M.S.P. and the Meat Transports was £515,000 odd?—No, I am not aware of that.

If those figures are right it means that it would be all wrong to imagine that in 1923 the figures were finally settled?—I obtained my information from a letter written by the chartered accountants in Liverpool, dated 28th December, 1923, to the company. The letter stated that the writers had prepared an estimate of the liability for 1920; that, taking the figures so far as they were agreed with the Inspector of Taxes, together with the claim for deferred repairs, and making ample provision for further adjustments, they considered the liability would not exceed £130,000.

What was it in that letter that you, qualifying yourself to give evidence in this case on the point, relied on?—That the amount provided in the books was in excess of the liability as estimated in that letter.

Were you under the impression, before the case started, that the R.M.S.P. in 1926 and 1927 were drawing on old reserves?—I was.

## Evidence for Prosecution.

Sir William M'Lintock

In your deposition you say that the companies brought in transfers from old reserves. That was based on what you said in your report "large transfers from old reserve accounts"?—Yes.

Are you now satisfied that, as regards the income tax contribution to begin with, it arose in the year in which it was transferred?—I am satisfied that there was a sum recovered which had clearly gone to the credit of profit and loss account.

Are you satisfied that the same thing is true about 1927?—For income tax, yes.

Are you satisfied now that it was a misapprehension to suppose that there were figures finally settled in 1923 in regard to E.P.D., and, on the contrary, that very much larger amounts were subsequently substituted?—No, I do not agree.

I refer to a letter dated 7th March, 1925, written by the Inland Revenue to the R M S.P. Company. The writer there says that it appears that the adjustment of the company's liabilities is still so far from settled that he is afraid nothing can be done in the way of approving a further interim repayment at that time. Do you not now agree that, if the situation were as disclosed by that letter, it would be difficult to describe the funds as old reserves, as though they had been free to be drawn from long before?—It is only fair that I should indicate exactly what I had in front of me when I excluded them as part of the earnings of these particular companies. I was dealing with current earnings. The R.M.S.P. had made provision, during the seven years referred to, amounting to £2,260,000, as the possible liability. The ultimate total liability was £1,773,000.

In what year was that fixed?—The matter was reopened and finally agreed in 1927. They had obtained an obsolescence allowance which was set off against the ordinary calculations as to the liability of £1,187,000, so that the net liability was, in round figures, £600,000, but they had provided £2,260,000 during the seven years. That was my justification for stating that the sum carried from that over-provision had nothing to do with the earnings of either the years 1926 or 1927.

That is a very clear explanation, to which I will refer later, when addressing the jury. Remember that you are testifying in a criminal charge. Is it your evidence that, as regards any transfer from E.P.D. account in 1926 or 1927, the company, at the time they made that transfer, were consciously drawing upon what were ascertained to be old, free reserves?—Yes.

That is your evidence now?—Yes.

Let me suppose for the sake of argument that a company in a bad year does draw upon old reserves and does assist to make it possible to distribute a dividend by so doing. There is no doubt, is there, that if the reserves are free, they are legitimate subject-matter for distribution?—I do not know.

They are undivided profits?—Yes.

When one speaks of a company as equalising or seeking to equalise its dividend, it means, does it not, that during a period of good years

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Sir William M'Lintock

it does not distribute all it might in order to assist it in bad years?—Yes.

There is just one thing more. Will you look at Exhibit No. 59? It is called "Balance proof, income tax reserves" As I understand it, these entries are in the books of the R.M.S.P. I think this particular exhibit has been prepared by Mr. Matthews. I think it will show an internal calculation as to what the reserve would be in any given year. It shows, does it not, that the only part of the income tax reserve which was regarded as surplus or free at the beginning of the year 1926 was £99,000?—That is what that note would convey to me. The balance of it was owing.

In other words, if you wanted to know what it was at the beginning of the impeached year 1926, it would appear that at the most it was £99,000?—Yes.

Do you get a surplus reserve twelve months later of £208,804?—Yes.

And that is after taking out in the course of the year and paying over to profit and loss account the £175,000? Is not a fair inference from those two documents this—that, so far from drawing steadily out of this account and depleting it, as a matter of fact in the calendar year 1926 the free surplus reserve was substantially increased?—Yes, from £99,000 to £208,801.

And that, after drawing out £175,000?—I assume that, though that statement does not show it. This is a specially compiled document, trying to show the true tax liability.

As you pointed out, these very important figures represented by the E.P.D. are really figures that are common to the R.M.S.P. and the subsidiary companies?—Yes, they were settled as a whole—as one unit.

It follows, therefore, that questions that I have been putting to you about E.P.D. and similar matters, though I have put them with reference to the Royal Mail Steam Packet Company, really apply to the group?—I think that is a fair way to put it.

So I need only put this further to you. You have pointed out that dividends were paid by these 100 per cent. subsidiaries. Confining yourself to these subsidiaries, do you know that after paying these dividends the subsidiaries were left with very large reserves? I will, if you like, give you a figure?—I was going to say that generally the result of the knowledge I had is that nearly all R.M.S.P. companies have still got in their books very large reserves.

And when you say "got in their books," let us have it quite clear, this is not a case where anybody suggests that they are not honest records?—Oh no, not for a moment.

In 1926 these 100 per cent. owned subsidiaries, according to the document before me, had a total reserve of £1,150,000, and in the year 1927 £1,100,000?—That is the aggregation of the reserves appearing in the books.

## Evidence for Prosecution.

Sir William M'Lintock

Of the 100 per cent. companies only?—Yes. I am doubtful if the ships are worth the money they appear at in the accounts.

By the COURT—Actually the existence of reserves depends on whether the assets are truly balanced on the other side?—That is so.

They are not free reserves, they are not immediately realisable?—They are free reserves in the general sense, but it is all invested.

All invested in ships?—Yes.

*Cross-examination continued*—You have had to consider with the holders of the Second Debentures whether or not their Second Debentures are covered by assets?—Yes

I may take it, may I not, that, with the appointment of the voting trustees, and the general publicity there has been, that for the time being at least there has been a depreciation in value if it came to a forced sale?—Oh, yes, undoubtedly.

Cross-examined by Sir PATRICK HASTINGH—We have been told that you conducted an inquiry into the affairs of the R.M.S.P. group?—Yes, of a limited character.

And did that take you a very considerable time? Did your inquiry take some time?—Yes.

During that time did you ever ask Mr. Morland for any explanation of anything he either did or did not do in relation to his duties as auditor?—No, I did not. I did not meet Mr. Morland himself, but my assistant in the course of his work was in touch with Mr. Morland's assistant, and I was furnished with documents.

Did you personally ever ask Mr. Morland for any explanation of any kind of anything that he did or did not do?—I did not.

Mr. ARTHUR THEODORE CANON, examined by Mr. EUSTACE FULTON—From 1913 until May, 1931, I was chief accountant of the R.M.S.P. Company. Before 1913 I was assistant accountant to the company. The company's accounts from 1913 were kept in London under my supervision as chief accountant.

Early in 1927 was a draft of the profit and loss account for 1926 prepared?—I think it was earlier than that.

What date do you put it at?—The rough draft are you referring to?

I am talking of the draft which followed upon the estimate which you got out just before?—I should think some time in March.

Just look at Exhibit No. 6, will you? That document is described as an estimate of 1926?—Yes.

Is that the first draft that was prepared of the profit and loss account for that year?—Yes.

That is the estimate, is it, of the company's trading, and does it show that you are looking forward to a possible deficit of £1,100,000?—Yes. This document is an estimate of the trading of the company. The company is really 75 per cent. investment and 25 per cent. shipping, and therefore it is reasonable to take the document as a whole.

And what does the estimate show?—It shows a deficit of £1,100,000.

Which would be increased, I understand, if the Ordinary dividend of 4 per cent. was paid?—Yes.

# The Royal Mail Case.

Arthur T. Cason

How did you come to prepare that document?—At the request of Lord Kysant.

When you showed it to Lord Kysant upon 12th October, 1926, what did he say to you, if anything?—He asked me what unpublished reserves we had got and how we could meet the deficit

When you showed the document to Lord Kysant, were those figures on the right-hand side—unpublished reserves and other things—upon it?—I cannot remember. I think that they were not I agree that the figures in question include an item of unpublished reserves £600,000, and the total given is over £1,144,000

Looking just below those figures, you will find on the same side of the document some figures which are written smaller. Can you tell me whether those were written in at the same date or at some later date?—At a later date.

Tell us what those figures represent?—Those are the details of the £600,000 unpublished reserves. During the war the company ran certain ships on behalf of the Government, and what is shown is the balance which remained out of the allowances which were made.

You have told us that Lord Kysant asked you to ascertain what reserves there were. After you had ascertained, did you communicate to him what you had found?—Yes.

I notice an item "Bonus shares from Nelson's." How did you come to put that there?—Lord Kysant told me that he was going to declare a bonus of £200,000 from one of the Nelson companies.

The deficit being £1,300,000 when you came to make up the profit and loss account, what did you take from those reserves, if anything? How much was it?—The figures were income tax, £175,000, and E.P.D., £550,000.

What is the total?—£725,000 on those figures, and the reserve fund is shown separately in the printed account—£150,000.

Did you show that document to Lord Kysant?—No.

On whose instructions did you take those items from reserve and put them into profit and loss?—On Lord Kysant's.

Does the same book that you have got before you contain also the balance sheet for the company as at 31st December of that year?—Yes.

That is signed by Lord Kysant as chairman and also by the secretary of the company?—Yes

Does it contain the auditors' report signed "H. J. Morland"?—Yes.

The document that follows it is the final profit and loss account for the same year?—Yes.

Just looking at the details of the profit and loss account which you have there in the final form as prepared, do you find against the items auditors' ticks?—Yes.

Do you know of your own knowledge who was the person who dealt with those accounts and put those ticks upon them?—I am not sure who made the ticks; the auditing was under the jurisdiction of Mr. M'Arthur, and I think it was one of his assistants who made the ticks.

## Evidence for Prosecution.

Arthur T. Cason

In what item are transfers from reserve shown in the profit and loss account?—The £725,000 which has been referred to was taken from the item of the previous year, sundry balances.

Referring to the printed annual reports of the Company for the period 1921 to 1925, you might look at the reports for 1921 and 1922. I suggest that in each of them, in the profit and loss account, there is set out on the right-hand side an item of profits for the year, including dividends, and so on?—Yes.

You find the word “profit” being used in those two years?—Yes.

In 1923 you find the words are the same, except that the word “balance” has been substituted for the word “profit”?—Yes.

In 1924 the words are unchanged as from 1923?—Yes.

Looking at 1925, do you find in that year after the words “allied and other companies” the insertion of the words “adjustment of taxation reserves”?—Yes. In 1926 and 1927 the form of words used was unchanged as from 1925.

On 4th May, 1927, was there a meeting of the board of directors held to approve of the profit and loss account for 1926?—Yes.

At that meeting Lord Kysant was present, but I think Mr. Morland was not?—No.

Now look at Exhibit No. 13. Was that the document put before the court, which is in effect the final court before it goes before the shareholders?—There might be some slight alterations.

That is a document which is put before the board, subject to audit?—Yes.

Apart from the information contained in that document, was any other information given to the court?—Not in my presence.

Were you present at the whole of the meeting?—While the accounts were being discussed.

While the accounts were being discussed in your presence was anything said about bringing into the account the secret reserves or any other information regarding assets?—No.

Going now to the year 1927, was an estimate prepared in the same way for that year as for 1926?—Yes.

Look at Exhibit No. 14. I notice that at the top of the right-hand corner is the initial “K.” Was it Lord Kysant’s practice to initial documents in that way when they had been before him?—Yes.

That document now has figures in black and red upon it. Were they upon it when the document went before Lord Kysant?—No.

Which figures were upon it when he saw it?—Only the black.

When did you come, if you did, to write the red figures upon it?—The red figures are of a much later date.

How did you come to put them there?—I put them there as a check on what I had originally given. The figure of £382,905 covers three things. The income tax reserve originally stood at £200,000.

Having got out the final figures, will you look again at the memorandum you prepared for the auditors (Exhibit No. 15)?—Yes.

On the second folio I find there on the credit side two bonuses of

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Arthur T. Cason

the Nelson companies amounting in all to £300,000. Is that right?—No, it does not show that.

They are there?—Yes, they are part of the items “ interest on investments.”

What happened about that? Tell us in your own way?—The Nelson lines—H. & W. Nelson and the Nelson Steam Navigation Company—each declared a bonus—£100,000 in one case and £200,000 in the other—and these were taken credit for in “ interest on investments.”

In that year?—In that year

In your estimate, the one you have just produced, was income tax reserve, &c., shown at £382,905 You have told me about it, and that the “ &c.” was in red?—Yes

Did income tax reserve in that figure stand at £200,000?—No, at £120,000.

What happened then?—The other items which are just below the “ interest on investments ” include corporation profits tax, £32,905; excess profits duty, £230,000, which make up the £382,905. The actual excess profits duty was taken finally at £232,787 19s. 1d.

Were those items taken from reserve and put into profit and loss?—Yes.

Upon your own motion or instructions?—Instructions.

From whom?—Lord Kylsant

Now just tell me the company's practice with regard to depreciation?—The company's practice was to write off a ship after twenty years' life.

Looking at Exhibit No. 14, I find there an item of £170,300 depreciation not to be charged. Why was that?—Because we had in the previous years written off more than the 5 per cent depreciation.

Was that how you had it in hand?—We had in hand more than that.

In point of fact, it appears that the £170,300 was not taken in?—Yes.

How did that come about—did you have any conversation with anybody about it?—It was not necessary.

You have told me that with regard to the Nelson £200,000 that that sum was put into the books and taken out again. Was that done by anybody's instructions?—On Lord Kylsant's.

Referring to Journal E., do you find an entry dated 31st December, 1926, with reference to interest on investments, £200,000?—Yes. This was subsequently cancelled.

On another folio under date December, 1926, do you find investments in allied companies of £200,000 were again cancelled at a subsequent date?—Yes.

On folio 363 do you find an item on the credit side under December, 1926, “ interest on investments,” and again the sum of £200,000 and cancelled at a subsequent date?—Yes.

Look at Exhibit No. 14. Do you find there a profit on the sale of H. & W. Nelson of £200,000?—Yes.

## Evidence for Prosecution.

Arthur T. Cason

Will you tell us about the transactions by which H. & W. Nelson was sold to the Nelson Steam Navigation Company—how that came about?—Lord Kysant thought it desirable that the management company—H. & W. Nelson, Ltd.—should be owned by the steamship company. It was, therefore, put to the board in that way and arranged that the holding of the R.M.S.P. Company should be sold to the Nelson Steam Navigation Company, so that it would be a self-contained unit.

How was the price fixed?—It was fixed at the par value of the whole of the shares which had been issued to the company

In 1927 was a general balance sheet and profit and loss account prepared as before—have you the document that was put before the court of directors?—Yes

And prepared in the same way as the others, showing the figures for the preceding year, 1926?—Yes.

Were you present at the meeting of the court of directors at which it was produced?—Yes.

In your hearing was anything said as to the movement from reserves into profit and loss?—No.

By the Court—Had the company made a profit on its trading? Was any question asked about that?—No, my lord.

Was any question asked about the sundry credits or the adjustment of taxation reserve?—No.

Was no question raised on the balance sheet or the profit and loss account at all in your hearing?—Yes, in 1927 there was. One of the directors asked: "What do the auditors say?" I had already seen the auditor

*Examination continued*—Who, Mr. Morland?—Mr. Morland personally, and I replied, on being indicated to do so by Lord Kysant, that the auditor said there was no technical objection.

Was that stated by Mr. Morland, or not?—Yes.

Was there any further discussion?—No discussion on the accounts. Before this Lord Kysant gave a short summary of how the 100 per cent. companies had been doing, but that had no connection with the account other than to satisfy a question which I understood had been asked at a previous board.

You said something about Mr. Morland. Will you give us the conversation you had?—Before the accounts went to the board I went to see Mr. Morland to see if there were any technical objections.

By the Court—Did you just ask the question in that form, or did you say what the technical objection might relate to?—No, I simply said "technical objection," and put the document before him. It was particularly in relation to the Nelson Line bonus.

*Examination continued*—Did you indicate any part of the document to him before asking the question?—I pointed out the item.

By the Court—What document was it you were showing to Mr. Morland?—I do not have it. It contained figures which particularly referred to the bonuses from the Nelson Company.

And you asked if there were any technical objections, and then he gave you an answer?—Yes, that there were no objections.



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Arthur T. Cason

And then at the meeting some director came to ask if there were any technical objections?—No, all that the director said was “What did the auditor say?”

Had that reference to anything that had been said at the meeting? He simply said that quite suddenly?—Yes.

And you repeated what Mr. Morland said?—Yes.

And did the discussion continue on that, or did it stop?—It stopped.

*Examination continued*—You showed that document to Mr. Morland. What did you say?—I said “I don’t like it.” I understood him to say “Nor I.”

Was Exhibit No. 20 before Lord Kysant at that meeting? It bears his initial?—Yes. After those documents have been put before the board, in the ordinary course they go before the auditors, and in their final form they bear upon them Mr. Morland’s signature. I have got before me the final form of the balance sheet for that year and the profit and loss account. With regard to each of these years, while I was present the accounts went before the directors, but no information was given to them about these movements in the profit and loss account. I was also present in the years 1921 to 1925.

Was any information of that character given in your presence at any of those meetings?—No.

By the COURT—Did none of the directors ever ask if the company was earning any profit or not?—No.

*Examination continued*—Were you in the habit of keeping a summarised document of the details of profit and loss covering a number of years?—Yes. I produce Exhibit No. 21, which is a copy of the document I originally had.

That shows the surplus or deficit each year?—Yes.

This document begins in 1920 and ends in 1929?—Yes.

Was that a document you kept for your own private information?—Yes. It was taken by Mr. M’Arthur to Mr. Morland, but whether he saw it or not I don’t know.

From the years 1921 to 1927, to go no further, were there in each year special credits taken into account?—Yes.

Can you tell me whether Lord Kysant was aware of that?—Yes.

Did he approve of it or not?—Yes. In April, 1928, I went away for my holiday. There is a document dated 13th May, 1926, which is headed “Memorandum from the Accountants,” and is addressed to the chairman. It states that Mr. Morland had signed the balance sheet subject to approval of an alteration in the profit and loss account as per rough proof attached.

Can you tell us what the contents were?—Yes, it contained the alteration in the wording with reference to the item of dividends of allied and other companies, less depreciation of freight, &c.

Take 1922, do you find the same wording in the profit and loss account for that year, except that the word in that year is “profits”?—Yes.

So that in these two years the wording is exactly the same, except

## Evidence for Prosecution.

Arthur T. Cason

that in 1923 you get the word "balance" instead of "profit." Can you tell us how that came about?—Lord Kyslant required it to be altered.

I just want to deal with the question of the exchange of cheques between the Nelson Steam Navigation Company and the R.M.S.P. Can you tell me under whose instructions it was done, if anybody's?—Under the instructions of Lord Kyslant

Mr. FULTON—Will you now look at the letter dated 28th May, 1926?

Sir PATRICK HASTINGS—I understand that the evidence my friend is now calling does not affect my client.

Mr. JUSTICE WRIGHT—You are quite right. I was going to say something on this myself.

Mr. FULTON—All the evidence following relates to the prospectus charge in which Mr. Morland is not concerned

*Examination continued*—What is the letter of 28th May, 1926, addressed to the chairman of the R.M.S.P.?—That was from Barclays Bank in reference to their renewing the arrangement for the continuation of the company's overdraft of £300,000 for a further period of six months on the same terms as hitherto.

You will see it is quite clear that there is written in manuscript at the bottom in pencil—a part of the document—with the initial "K," "Mr. Cason. Have arranged to make this £500,000 till early next year"—Yes.

Was that written subsequently to the date of the letter?—Yes, about six months afterwards. On 3rd December, 1926, a letter was addressed to Lord Kyslant, signed by Mr. Fraser, general manager to Barclays Bank head office, informing him that it had been agreed to grant the R.M.S.P. an additional £200,000 overdraft, making £500,000 in all, and that they gathered it was the chairman's intention to pay the additional advance in three months from the proceeds of a public issue. There is another letter signed by the manager of Barclays Bank, dated 18th March, 1927, addressed to the secretary of the R.M.S.P. which bears the initial "K," and is in reference to the same matter.

The next document to which I wish to draw your attention is called "Memorandum for the chairman." Was that put before Lord Kyslant to your knowledge?—Yes.

You sent the original yourself to him?—Yes. There were a number of other letters with regard to the £500,000 overdraft, and it will be noticed that there was an extension for another three months granted.

Did you go for your holiday in 1928 towards the end of May or thereabouts?—Yes.

So far as you knew had anything been done then in relation to the prospectus or the issue mentioned?—No.

When you came back on 11th June, or about that date, did your assistant, Mr. Lewis, speak to you and show you some figures?—Yes.

When you saw that document, was it in its present form, because I see some pencilled words added at the top?—The pencilled figures were not there.

How did the pencil figures come to be added to the draft?—They

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are in my handwriting. I was called down to Lord Kysant's room in connection with the prospectus. I told Lord Kysant that we did not use the word "profits" in our accounts, but said "balance."

And what did he say?—He altered the wording in the paragraph at once. It was the draft prospectus.

Did you have any other discussion with Lord Kysant with regard to the preparation of the prospectus?—No. I produce a summarised profit and loss account of the Meat Transports Company from 1918 to 1929, which shows that the transfer from reserve was £25,000 in 1926 and £25,000 in 1929. The transfer from the taxation reserve in 1926 was £37,500, in 1927 £25,251, and in 1928 £8000. The transfers were brought forward on the instructions of Lord Kysant, and they appeared on the balance sheet and were passed by the board. I also produce the signed balance sheets of the company for 1926 and 1927.

Was Mr. Morland dealing with the accounts of that company, on behalf of Price, Waterhouse & Co., who were the auditors, as a firm?—Yes.

Who dealt with the accounts on behalf of that firm?—As a rule, Mr. Morland.

In these two particular years, who dealt with these accounts?—They were dealt with on behalf of the firm by the same staff who dealt with the Royal Mail accounts; the signature is obtained of the firm, and whichever partner was available would sign the account.

Who signed either of these documents?—In 1927 the signature is Mr. Morland's; I am not sure whose the signature is in 1926.

It only appears as Price, Waterhouse & Co.?—Yes.

What were Lord Kysant's drawings?—In 1920 Lord Kysant drew £48,337. In 1922 the figure was £23,376, in 1923 £26,045, 1924 £26,490, 1925 £27,165. In 1926, when the dividend fell to 4 per cent., Lord Kysant drew £3000. In 1927 he drew £26,842. In 1928 there was a dividend of 5 per cent. declared, and I made provision in the books for Lord Kysant's half per cent. commission.

Did he, in fact, draw the amount he was entitled to?—No.

Why?—He did not wish to.

And did not, in fact, draw it?—No. In 1929 there was, in fact, no dividend declared, and Lord Kysant's drawing did not arise.

Cross-examined by Sir JOHN SIMON—At meetings of the board, the full board, were voyage accounts produced?—I believe so.

Did you have a particular line of ships, and did you have the figures showing whether there was a deficit or a surplus on the voyage, and how much the voyage would cost, and the figures for the previous year, so that they could be compared?—That does not embrace the whole of the company's fleet, only the voyages which are run trans-Atlantically.

Would it include the Brazilian and River Plate "A" Line, the North Atlantic Line, the West India Cargo Line, the Brazil Cargo Line, the North Atlantic Line, the Canada and West Indies Line, the River Plate Cargo Line, and the Norwegian Cruises?—Yes.

## Evidence for Prosecution.

Arthur T. Cason

What is it that would be the most important example of things omitted?—The ships lying up and the amounts that do not go down to voyages.

What I wanted to get quite clear from you was that the whole board, these distinguished gentlemen, directors drawing fees, had before them as they attended the meetings of the board, a summary of the voyage accounts stated in the case of each separate ship as far as the Atlantic Lines and the like go, whether the result was a deficit or a surplus, how much the repairs were, and how it stood in comparison with the corresponding voyage in the previous year?—Yes. That is so.

By the COURT—Were you present at the board meetings?—No, except when the accounts were discussed. I think perhaps the secretary, who is to be called to give evidence, can state exactly what happened at the meetings.

The Court adjourned.

# The Royal Mail Case.

Third Day—Wednesday, 22nd July, 1931.

## Evidence for the Prosecution—Continued.

ARTHUR THEODORE CASON, further cross-examined by Sir JOHN SIMON—I would like to remind you of an answer you gave yesterday to a question you were asked about the Nelson matter of £200,000. I am looking at your evidence before the Lord Mayor at the Guildhall, and I see that you were asked a question about it, and this is what you said before the Lord Mayor. "It was decided that the Royal Mail Steam Packet Company should sell H. & W. Nelson, Ltd., to the Nelson Steam Navigation Company. Lord Kysant decided that, with the approval of the directors"—That was what I said

And that is correct?—Yes.

And the members of the jury may take it that it was not a matter which Lord Kysant decided alone, but a matter brought before the court and approved by the directors?—Yes, on the initiative of Lord Kysant.

Lord Kysant was managing director and he would have, no doubt, the main responsibility for initiating the proposals?—Yes.

You are not suggesting that the decision was merely his decision; it was approved by the board, I take it?—Yes.

MR. JUSTICE WRIGHT—Which year does this refer to?

Sir JOHN SIMON—It comes in 1927.

*Cross-examination continued*—When you spoke yesterday, your answer was in relation to an entry in the book, afterwards struck out, and the year of that was 1926?—Yes.

The matter that was carried through, and carried through with the approval of the directors, was in 1927?—Yes. It was in the year 1927 that the one Nelson company provided £200,000, and the other company £100,000.

Had the two Nelson companies the money to pay the £300,000 in 1927?—Yes.

1927 was a year when you had some conversation with Mr. Morland about something being technically correct?—Yes.

It is called a bonus of £200,000?—Yes.

See if your understanding of that is the same as mine. That would mean that the Nelson company had at that time, having done exceedingly well, a very large fund which was available for distribution, and it might have been disposed of by declaring a higher rate of dividend?—Yes.

And it declared an ordinary rate of dividend and the rest was declared as a bonus?—Yes.

It was never more than a name for a good lump of profits paid over as one thing?—Yes.

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Arthur T. Cason

You satisfied yourself that that was technically quite correct?—Yes. I agree that the shares in the Nelson company were owned by one shareholder. It therefore did not matter whether they divided the lump sum of profit in a lot of little bits or whether it was handed over as a lump sum. As I understood the matter, the £200,000 of the one Nelson company was distributable profit. Instead of the distributable profit being distributed as a dividend of so much per cent., it was distributed in part by dividend and in part by a lump sum.

And, in the same way, the other Nelson company paid over the £100,000 to the shareholder, the R.M.S.P. Company, as a lump sum?—Yes.

You told us yesterday that you had been the chief accountant of the R.M.S.P. since 1913, and you said that before 1913 you had been assistant accountant. So I have in the witness-box a gentleman who at the time was connected with the accounts of the R.M.S.P. from 1911 down to the time when you retired?—Yes.

Are there figures at the bottom of the exhibit which you have in your hand setting out what dividends on the ordinary stock have been paid, and are the figures correct?—Yes.

Looking through this series of twenty-two years, and observing the figures of dividends, was it the practice of the company in more prosperous years to pay a smaller dividend than would have been possible, so as to have undistributed profit in years that were less profitable?—Yes.

The rate of dividend in 1911 was 5 per cent. Am I right in my information that in order to pay that dividend of 5 per cent. £45,000 would be taken from profits?—Yes.

In the year 1911, was there £45,000 of profits available for distribution?—Yes.

How much more profit had the company in 1911 which it did not distribute? How much did it add to the reserve fund?—£40,000.

How much in that year in addition did it pay to the insurance fund?—£40,000.

So that it had paid all prior charges and all its preference dividends, and after it had paid 5 per cent. on its ordinary shares in the year 1911, it increased its published reserves by £80,000?—Yes.

If £45,000 is enough to produce a dividend of 5 per cent., £80,000 would be enough to produce 8.8 per cent.?—Yes.

And, if we add them together, in the year 1911, which was a prosperous year, if the R.M.S.P. had not followed the conservative policy of putting £80,000 of its profits aside and not distributing them, it might have paid a dividend of 13.8 per cent.?—Yes.

For the year 1912 the rate of dividend was 6 per cent., and that dividend would call for approximately £87,000?—Yes.

Could you tell me how much in that year was available for distribution if nothing more had been carried to reserve? I think you will find that in that year there was carried to the published reserve fund a further sum out of profits of £130,000?—Yes, that is so.

# The Royal Mail Case.

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And there was also carried to the insurance fund a sum of £40,000?—£47,000 is the figure.

The result being that there was available in that year, if a less prudent policy had been followed, not £87,000, but £257,000—over a quarter of a million?—Yes.

And that, as I work it out, means that in the year 1912 Lord Kylsant and the board might have distributed not 6 per cent., but 17.7 per cent?—I take it from you that calculation is correct; it is obvious it must be.

In 1913 the dividend declared was 6 per cent., involving approximately £151,500, and £10,000 more was put to reserve. A dividend of 6½ per cent. would have been justified?—Yes

Now in 1914 no dividend was paid?—No.

No money was distributed in that year, but it was necessary to withdraw from the reserve fund £200,000. In 1915 the money which had been withdrawn from the reserve fund was put back again.

And having kept things level in very difficult times, it was decided to restore the reserve fund again?—Yes.

In 1915 a dividend of 6 per cent. was paid. The company might have paid 7.8 per cent. The dividend payment called for a sum of £198,000?—Yes.

And in addition £200,000 was put back into the reserve fund, and was £58,375 put into the insurance fund or added to the reserve of the insurance fund?—Yes

With the result that instead of paying 6 per cent. the company might in that year have paid 7.8 per cent.?—Yes.

There is rather a striking contrast here. Do you realise that in the year 1915 Lord Kylsant and the company put aside out of distributable profits to reserve more than the total amount which they distributed in dividends?—Yes.

That was putting something aside for a rainy day, in fact?—Yes.

In the year 1916 the amounts available for dividend could have paid 13 per cent., when, in fact, 7 per cent. was paid, and in the following year, 1917, the dividend could have been 13.4 per cent., in 1918 11.8 per cent., in 1919 18.5 per cent., and in 1920 17.7 per cent.?—Yes.

It is quite plain, is it not, that the practice of this company was this: that over a series of years when the cycle of trade gave prosperity, full advantage of that prosperity was not taken, but very large sums were set aside lest a worse day should come?—Yes

And do you agree that such sums are set aside in order that they might be used when bad times arrive?—Yes.

Do you agree that in 1921, when the dividend paid was 6 per cent., the divisible profit might have justified 9.4 per cent.?

MR. JUSTICE WRIGHT—What do you mean by that?

SIR JOHN SIMON—If there had been no further transfers to the reserve fund. If in the year 1921 nothing more had been put to reserve the result would have been that instead of there being only 6 per cent. the dividend might have been 9.4 per cent.

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*Cross-examination continued*—Let us see what the situation was when the year 1921 began. In the previous ten years there had been added to the reserve funds, as I have mentioned, very large sums?—Yes.

And in those ten years there had been an increasing free surplus on the insurance fund built up?—Yes.

In 1921 nothing was drawn from the published reserve fund?—No.

Was anything withdrawn from the insurance fund?—No, I think not.

Was there in fact £172,636 added to it in that year?—Yes.

And in that year some special credits came in, and those special credits, together with the trading of the year, allowed 6 per cent. dividend?—Yes.

In fact, if £172,000 more had not been put into the insurance fund, it might have been 9 4 per cent.?—Yes.

In the year 1926 was there a drawing out of the published reserve fund of £150,000?—Yes.

Although in the same year the insurance reserve fund increased by £14,404?—Yes, that is so

So when you come to the year 1926, if you did not take advantage of the conservative practice of previous years, the dividend available could not have been 4 per cent. but only just under 2 per cent.?—That is so.

MR. JUSTICE WRIGHT—As far as I have followed the case, there appear to be certain years in which there were no profits. There were no trading profits of the R.M.S.P., although there were certain profits from investments.

SIR JOHN SIMON—There were two sources. There were payments—dividends from investments—and sums which might have been expected to be wanted to meet claims such as Inland Revenue, and which were found in a good year not to be required. That really was the same thing as an addition to the profits of the year. If from the beginning of the year it was ascertained that no claim would arise, then, *pro tanto*, the sum set aside was available for profit and distribution. An even more important point, strange though it might appear, is that in the difficult years the company was receiving from the Revenue actual accretions.

MR. JUSTICE WRIGHT—Yes, that appears

SIR JOHN SIMON—I put the document before your lordship and the jury as I realise that it will be more convenient for them to follow a tabulated statement. I am not seeking to exclude from the case what has been called the E.P.D. and income tax credit. I am not suggesting that they come into the document now before the Court. That document is limited solely to the two published reserves. One is reserve fund and the other the free excess which was continually growing under the heading of "insurance." In the table an endeavour is made to set out year by year, from 1911 onwards, the rate of dividend paid by the company, together with the actual amount needed for that purpose. The dividends paid are set out in the prospectus. The document also shows the increase in the published reserve funds.



# The Royal Mail Case.

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*Cross-examination continued*—The document also shows the total amount of the insurance fund at the end of each year?—Yes.

I would call attention to the fact that in the course of the period from 1911 to 1927 it has grown from £300,000 to £1,311,759?—Yes, that is right.

In the balance sheet of 1927 it appears at £1,311,000?—Yes.

This document does not contain on the face of it any of those sums we have heard of in 1926 and 1927, which were called "income tax reserve" and "E.P.D."?—No.

Is not the reason for that that the sums which you find in those ledgers were really what I may call invisible undistributed profits? They were put aside, and they might have been needed contingently to meet a liability?—Yes.

When it turned out that they were not wanted to meet a liability, they became undistributed profits?—Yes

Am I right when I say that those income tax and E.P.D. figures were over and above the reserves mentioned in this document?—Yes.

Am I right when I say that these sums for income tax and E.P.D. have all been created out of undistributed profits?—Yes.

The position is that when in 1926, for example, there is brought in for that year £175,000 from the income tax account and £550,000 from the E.P.D. account, those sums have all been provided out of undistributed previous profits?—Yes.

Assuming when they are brought into the profit and loss account and distributed that they are free, there is no reason known to you why you should not distribute undistributed profits which are free to be distributed?—No.

You were not in Court when Sir William M'Lintock gave his evidence. In the course of his evidence Sir William M'Lintock had pointed out to him, and agreed, that in fact £175,000 income tax brought into the profit and loss account for the calendar year 1926 might be regarded as made up of sums which were received in 1926?—I am not clear on that matter.

I show you a summary of the income tax reserves and call your attention to an item of £121,237, tax deducted from dividends paid. That means that in the course of 1926, when dividend warrants were prepared, the company deducted the proportionate amount of income tax, and did not pay the shareholders the gross declared percentage?—Yes.

Mr. JUSTICE WRIGHT—The tax is deducted from the dividend paid. That means that the company enters 5 per cent. as having been paid, but actually pays 5 per cent., less tax, and therefore credits itself with the balance.

Sir JOHN SIMON—It keeps what it deducts.

Mr. JUSTICE WRIGHT—It credits itself, and rightly credits itself. It is a deduction it is entitled to enter.

Sir JOHN SIMON—It is what the law calls, "the proportionate amount."

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*Cross-examination continued*—It sometimes happens that in a good year the company received more than it had to account for to the Revenue. In other years it might get less. That credit of £121,000, to which I have referred, arose from the fact that in the year dividends had been declared and warrants posted. There was also a sum of £5170 cash obtained from the Inland Revenue as a refund in that year. An additional £70,000 in 1926 came from the Revenue in view of the fact that the R.M.S.P. was not making the profit it had earned in previous years?—Yes.

Those three sums of £121,000, £5000, and £70,000 are free credits which arise in the year 1926?—Yes.

They amount to a total of £196,000?—Yes.

If you are fortunate enough to get back from the Inland Revenue something under E.P.D. account, you will have to account to them for rather more in the way of income tax than you had hoped to do?—Yes.

It is an advantage to the company on the whole, but they have to account for income tax on the difference?—Yes. The deduction in 1926 amounted to £13,000, and so in 1926 the repayment was £180,000. It therefore seems to follow that £180,000 arose out of the year 1926 in the income tax account. In that year £175,000 was transferred from the income tax account to the profit and loss account.

As a matter of fact, at the end of the year 1926 there was a larger credit balance in the income tax account than there was at the beginning?—Yes.

It is obvious that it is not a case of depleting some ancient reserves, it is a case of transferring in 1926 sums which have arisen within the year 1926?—That is so.

I desire now to address a series of questions on a very long document which has been produced. It might be described as “a panoramic view.” The first thing one notices about the document is that in point of time it does not go so far back as the table I have produced, or as the prospectus. The latter goes back to the year 1911. I gather that you have spent a large portion of your professional life in very close contact with shipping as an accountant. Have you ever heard of the view entertained in that branch of commerce, among others, that there is what is sometimes called a cycle of trade?—Yes.

I am not professing to understand it, but it means that experience goes to show, in connection with such a thing as the great shipping industry, that you do not get one good twelve months followed by one bad twelve months, but you get spread over a certain number of years a period of prosperity, a boom, if you like, followed unhappily by a period which is one of depression—a sort of graph?—Yes.

I am not asking you as a scientific student of the subject, or as an economist, but as a practical man in shipping—has a cycle of something in the neighbourhood of seven years been about right?—It is rather difficult to say so.

By the Court—Do you know?—No.

*Cross-examination continued*—There were some very prosperous years prior to 1920?—Yes.

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Years in which prudent and conservative management would suggest that you should set aside a portion of your earnings for the year rather than spend it all in those times of prosperity?—Yes.

And it becomes, does it not, a matter of very great importance when one is watching the general trend to see that there are indications in the figures which might suggest some return to greater prosperity?—Yes.

Look for a moment at the published accounts of the R.M.S.P. for 1926, and turn to the directors' report. It is there stated: "For the first four months of 1926 there was a considerable increase in the quantities of outward cargo compared with the corresponding period of the previous year." Is that true?—Yes

That meant that British exports were going up?—Yes. I am not responsible for this report.

I daresay you remember what happened in the month of May, 1926?—The general strike.

This indication of recovery was necessarily uncertain and speculative?—Yes.

At any rate, the early part of 1926 had shown a most definite tendency to improve, and there was a considerable increase?—Yes.

Would this reference to the improvement at the beginning of 1926 be reflected in the voyage accounts, which went before the board?—Yes, but it only refers to outward cargo, and not to the whole business.

Assuming that to be correct, you would see the voyage account, and if voyages were becoming more profitable, that would be reflected in the voyage returns before the board?—Yes.

I show you a letter addressed to yourself from the Inland Revenue regarding the allowance for E.P.D. The letter is dated 7th March, 1926, and states: "It appears that the adjustment of your company's liability is still so far from settled, that I am afraid that nothing can be done in the way of approving a further interim repayment at present." On 18th May, 1927, more than two years later, the Inspector of Taxes in the City wrote another letter regarding the settlement of the E.P.D. payment. That letter states: "Final figures have to-day been seen, showing that the balance of E.P.D. to be repaid is £20,067. It is proposed to set this amount off against the overpayment of income tax." It further states that the amount of E.P.D. to be repaid amounted to £1,313,095. There were three payments in 1926, and the last three were "constructively," which meant they were set off against something else. You could not, having those letters in mind, have told anybody that the E.P.D. was settled in 1923?—No.

Cross-examined by Sir PATRICK HASTINGS—I want to know what practice was followed with regard to the yearly audit of the company's accounts. I suggest that every year, and during the year, the books of the company were kept by the regular accountancy department of the R.M.S.P. under you?—Yes. About the month of April in each year the clerks of Price, Waterhouse & Co. came in to check the accuracy of the books. My department prepared a balance sheet and a profit and loss

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account. The auditors' clerk checked the books after the account had been prepared.

By the COURT—You prepared your balance sheet, and then the clerks came in?—Yes.

*Cross-examination continued*—Up to that point Mr. Morland would not come to the office of the R. M. S. P. at all. The representative of Price, Waterhouse & Co. would check your figures, and you and your department would prepare a profit and loss account?—Yes.

The next thing that happened was that the profit and loss account prepared by you would then go before the board of directors?—No.

By the COURT—Before Mr. Morland came on the scene?—Yes, before Mr. Morland came on the scene.

*Cross-examination continued*—After that document was approved by the board of directors, then Mr. Morland would attend at the office, go through it, and, if he thought proper, certify it?—After his staff had checked it.

Mr. JUSTICE WRIGHT—I understand that the practice was for the auditors not to come on the scene at all until after the accounts had been prepared by the witness's department. The balance sheet and profit and loss account were drawn up and put before the board of directors, and approved by them. Then the assistants of Mr. Morland came on the scene.

*Cross-examination continued*—What happened in 1925, and how did the words "adjustment of taxation reserve" come upon the balance sheet in that year in the profit and loss account? Did Mr. Morland come to the office, and were there present, in addition to Mr. Morland, Mr. Lewis and yourself?—Yes. Mr. Lewis was my assistant accountant.

Had the profit and loss account, as well as the balance sheet, been before the board, and you had it to hand to Mr. Morland?—Yes.

Did Mr. Morland in that year state to you and Mr. Lewis that in his view the moment had arrived when it was necessary to indicate in the profit and loss account that the balance was arrived at after recourse to the E. P. D. reserves?—I don't remember that Mr. Morland himself said that.

Let me see if I can remind you. Take this document in your hands. That is an original document. So far as it is printed, did it contain the items which are brought into the profit and loss account for the year 1925 with no printed figures?—Yes.

Has some one written, in red ink, the figures which appear in the profit and loss account?—Yes.

Who wrote those figures?—I did.

On that print, which had been before the directors in 1925, was there any reference to the expression "adjustment of taxation reserve" in that document?—Not in the print.

The document which had been before the directors is the printed document?—Yes, but it is in a slightly different form.

The printed words are precisely the same as the printed words which appear in the final document without the words "adjustment of taxation reserve"?—Yes.

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Has somebody written in, in that document, the words " adjustment of taxation reserves " ?—Yes.

Is it written in ink or in pencil ?—In pencil.

In whose handwriting is it ?—I think it is Mr. Morland's.

Have you the slightest doubt that at that meeting between yourself, Mr. Lewis, and Mr. Morland, in the year 1926, Mr. Morland said, after perusing the balance sheet, which was put before the directors, that in his opinion the time had come when the notification that the E.P.D. reserve was being drawn upon should be indicated to the shareholders ?—I do not remember dealing direct with Mr. Morland in this connection, but there is no doubt that it is Mr. Morland's correction.

It was made in your presence, was it not ?—I do not remember it.

Do you notice that it is not even put in the right place in the balance sheet ?—Yes.

Mr. Morland wrote in, in pencil, " adjustment of taxation reserves " ?—That is so.

Does not that bring it home to your mind that it was done at the meeting between you, Mr. Lewis, and Mr. Morland, and that he said something to this effect: that in his view an indication must be given now to the shareholders that the E.P.D. reserves were to be called upon, and he there and then, in pencil, wrote it out in front of you ?—I am sorry, I have no actual recollection.

If Mr. Morland tells us that was so, you would not be in a position to dispute it ?—No.

Is it within your knowledge that Mr. Morland never saw Lord Kysant at all on these occasions at any time ?—I think he did at times.

There were some other companies in which Mr. Morland was also auditor ?—Yes.

In connection with these accounts of the R.M.S.P., I suggest that never did Mr. Morland see Lord Kysant at any time. Are you able to confirm that, or do not you know ?—I do not know.

You said yesterday, speaking about the time when you saw Mr. Morland regarding the bonus, and asked him whether there was any objection to it, you stated " I do not like it," and you understood him to say " Nor I " ?—Yes.

I do not quite know what you mean by " you understood him to say." Supposing Mr. Morland tells us that he never either formed a view or expressed any view about the matter, are you prepared to deny it ?—I should say he was mistaken.

You are not sure whether he did say " Nor I," or not ?—I cannot give you any help.

You said " I understood him to say ' Nor I.' " Does that mean that you may have misunderstood him ?—It is possible.

Re-examined by the ATTORNEY-GENERAL—With regard to the document which has been produced by Sir John Simon, and also the accounts of the R.M.S.P., going back to 1911, the document produced by counsel for the defence shows that, in addition to the payment of £45,000 in dividends, £80,000 was transferred to reserve. The accounts of the com-

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pany for that year show on the debit side of the profit and loss account what the company was doing with that money. There is an entry of "insurance fund account, transferred to credit £40,000," and also "reserve fund transferred to credit £10,000." Would any one, looking at the accounts for that year, see plainly on the face of the document that the company had put aside £80,000 to its reserves?—Yes.

Will you turn to the report of the directors? That states: "after making provision for depreciation, transferring £40,000 to the reserve fund, £40,000 to the insurance fund, and making the payment of the dividend on the preference stock, the court recommend a dividend of 5 per cent., less income tax, be paid on the ordinary stock"?—Yes.

Of course, for a company like this, the insurance fund is an important matter, is it not?—Yes, if you take some of the risks.

If you are going right out into the market, it does not matter, but, if you are writing some of your own risks, you must have a fund?—Yes.

By the COURT—I understand that the practice of the company was to insure 100 per cent against total loss and 75 per cent. against other losses with outside underwriters. That would not come into the insurance fund at all. The premiums paid to underwriters would be an ordinary disbursement of the company?—In the earlier years it was dealt with in that way. In later years a transfer has been made, and the premiums have been deducted against the fund.

As I understand, you kept an account of your fund, and that would show the amounts that you have appropriated to the insurance fund and the amounts paid out?—Yes.

But you always kept the surplus, and it was added to from time to time?—Yes.

Why did you do that? Was it to guard against the possible contingency of some very heavy loss or losses occurring which you insured yourself, or was it simply as an extra reserve fund?—The practice was to charge a certain percentage in the voyage accounts which more than covered the premiums which were paid out, and more than covered the risks which we had to meet.

They more than covered the losses you had to make good?—Yes.

And the result was that there was a gradual accumulation?—Yes.

*Re-examination continued*—Was the appreciation of the insurance fund due to a deliberate intention to increase it, or caused by the fact that the company took a certain percentage, and credited that amount constantly. I understood that the company would debit every voyage account with a certain amount for insurance?—That is correct.

How did you arrive at the figure?—I took a percentage.

A percentage of what?—Of the book value, but generally of the insurance value. In most cases the insurance value was higher than the book value.

What percentage was it?—Three per cent. until recently. Three per cent. is much too high.

Too high?—Yes, now.

By the COURT—The cost of repairs is not what it was?—That is so.

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*Re-examination continued*—From the beginning to the end, and from 1911 onwards, was the 3 per cent. the figure that was always adhered to?—Yes, until a good deal later. The 3 per cent. charge was made for a period of something like forty years, but safety at sea had improved so much that 3 per cent. was found to be too high a figure.

By the Court—It was a conditional figure?—Yes

*Re-examination continued*—And in 1922 it came down to what?—About 2 per cent.

The amount for insurance premiums worked out automatically at 2 to 3 per cent. ?—Yes.

Do you agree that the practice was to pay the premiums incurred for outside insurance from the fund, and also to debit it with the costs of any claims which had to be met under the company's own insurance?—Yes.

By the Court—Did the company have very heavy losses in any one year, say, running into hundreds of thousands of pounds, which it had to meet itself?—The risk was largely covered under the general average.

Mr. JUSTICE WRIGHT—Seventy-five per cent. would be covered outside, but 25 per cent. might mean a substantial amount.

*Re-examination continued*—Referring to the accounts of the company for 1924 and 1925, in the first of those two years the insurance fund stood at £1,215,000, and in the next it had risen to £1,256,000, or an increase of £41,000. Was that due to the automatic result of the operation of the 2 per cent. rule, or was it due to a deliberate increase of £40,000 to the fund?—It would be automatic.

In the 1912 accounts, it is stated "profit for the year after providing for depreciation of the fleet, &c., and including dividends and bonus on shares in steamship and other companies." A bonus is mentioned. What was that bonus?—If my memory serves me it was a bonus from Elder, Dempster & Co

Look at the report attached to the accounts. There, again, it says, "After making provision for depreciation, transferring £130,000 to reserve fund, £47,000 to insurance fund, £5000 to the pension fund, and deducting the amount of the half-yearly dividend on the preference stock, the court recommend the payment of the usual half-yearly dividend of 2½ per cent." Everybody concerned is told all about it, are they not?—Yes.

Take the next year. Look at the profit and loss account. Do you find there the transfer to the insurance fund of £37,000?—Yes.

Do you find that the transfer to that fund is £37,000, and the claims on the fund £27,000, and therefore the fund has gone up by £10,000?—Yes.

There, again, it is for everybody to read, and it is again mentioned at the bottom of page 10 of the report?—Yes.

In 1914 £200,000 was used. One is not surprised in that critical year, but it is all set out there for any one to see, and it is mentioned in the report?—Yes.

The next year it goes back again, and it is all set out for anybody to see, and mentioned in the report?—Yes.

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So that any one looking at the report would be able to see in one of these years what the insurance fund was, and what the general reserve was?—Yes.

And omitting for the moment any question of secret reserves, you see in 1926, as compared with 1925, although they had drawn on the general reserve to the extent of £150,000, yet the insurance fund had gone up slightly?—Yes.

By the COURT—How was the insurance fund represented? Was it in the form of assets? Was it an outside investment, or was it included in the value of the properties of the company?—It was represented by outside assets, my lord

Mr. JUSTICE WRIGHT—It was balanced by the valuation which appears on the assets on the balance sheet.

*Re-examination continued*—In a company like this no particular fund has earmarked assets. It is the account in the books, and the general assets of the company are responsible?—Yes.

Mr. JUSTICE WRIGHT—But some companies have outside investments.

*Re-examination continued*—It was not so in this case?—That is so.

Probably the insurance fund would be in ships, or part of the buildings of the company, or the goodwill?—Yes.

Taking the general balance sheet for the year to 31st December, 1925, anybody looking at that could see " Reserve fund £1,600,000 " ?—Yes.

Compare that with 1926. You see that the reserve fund has now become £1,450,000, having been drawn upon to the extent of £150,000, and the insurance fund has gone up from £1,256,524 to £1,300,000?—Yes.

That is available for any one to see?—Yes.

In addition you can see the profit and loss account for the year?—Yes.

The document put in by Sir John Simon had no regard whatever to the reserves which do not appear as such in the balance sheet?—That is so.

The other reserves would appear, if they are in the balance sheet, under the heading " Sundry balances " ?—Yes.

By the COURT—Somebody has produced a document called " Income tax account reserve." Would the annual balance on that account be included under the heading of " Sundry balances " ?—Yes.

That would be one of the items that go to make up the sundry balance?—Yes.

The item of sundry balances appears in the accounts of the company as far back as 1911. What was included in the item in that year?—It would include amounts for return tickets still to be availed of, deferred rebates, and passages which had been prepaid but not yet availed of, and the unpaid coal accounts, stores accounts, and provision accounts.

*Re-examination continued*—Comparing the build-up of the reserve in various years, from the balance sheet for the year 1925 there are items in respect of sundry balances, accounts not closed, and debts owing to the company, including loan from bankers, totalling £2,602,302. That



# The Royal Mail Case.

Arthur T. Cason

includes, among other things, various reserves. Assume that the E.P.D. reserve, which figured in that total, at that date was £390,277. The accounts for the following year show that the sundry balance item was £2,842,440, and I again ask you to assume that E.P.D. reserve figured at £110,277.

Were there, in the course of the year 1926, repayments of E.P.D. by the Inland Revenue, amounting to £330,000?—I have not the details. That matter will be dealt with later by Mr. Matthews (assistant accountant to the company) in his evidence.

Income tax in the years 1926 and 1927 was at the rate of 4s. in the £. Debenture interest, preference dividends and a 5 per cent. ordinary dividend represented a payment of about £700,000; if the company were paying over nominally £700,000, they could deduct from it at the rate of 4s. in the £ and retain that deduction, *i.e.*, a deduction of one-fifth. In 1926, however, the dividends were 4 per cent., instead of 5 per cent., and the payments amounted to £650,000; the deduction of one-fifth amounted to £130,000. In that year, if they debited the company with the payment of £650,000, they must automatically credit the company with the one-fifth, which is £130,000. The position that arose, therefore, was that the more they paid in dividends, and the less they paid in taxation, the larger was that automatic credit?—Yes.

Dealing with the insurance fund and general reserve fund, whereas in 1921 the former stood at £1,022,000, at the end of 1927 it was £1,311,000—an increase of almost £300,000. At the same time the general reserve fund was £1,600,000 in 1921, and it was £1,450,000 at the end of 1927. So that, considering the two funds together, they have increased to the extent of £150,000 between those two years. Those would be “bull points” in favour of the company?—Yes.

What was the position with regard to the undisclosed reserves as between 1921 and 1927?—They were much reduced.

The figures were as follows:—

## *E.P.D. Reserves.*

1922,	..	.	.	..	...	£100,000
1923,	.	.	.	...	...	100,000
1924,	..	...	...	...	...	330,000
1925,	.	...	...	..	...	300,000
						<hr/>
						£830,000
						<hr/>

## *Income Tax Reserves.*

1923,	...	...	...	...	...	£450,000
1924,	...	...	...	...	...	350,000
1925,	...	...	...	...	...	250,000
						<hr/>
						£1,050,000
						<hr/>

# Evidence for Prosecution.

Arthur T. Cason

Other figures are as follows:—

War contingency reserve,	£45,000
Corporations profits tax reserve,	40,000
Fleet depreciation fund,	444,000

Do you agree that these various reserves totalled some £2,800,000?—Yes.

Do you agree that in the years 1926 and 1927 the E.P.D. reserves were £550,000 and £232,000 respectively, making £782,000; income tax reserves were £175,000 and £120,000, making £295,000; the corporation profits tax reserve was £32,000? These amounted to more than another £1,000,000, so that reserves amounted to £3,800,000. Thus there had been expended, between 1921 and 1927, over £3,800,000 from the secret reserves, and it is legitimate to point out that the sum total of the disclosed reserves had increased by £150,000?—I agree.

Sir JOHN SIMON—The prospectus gives the figures from 1911 onwards, but the Attorney-General has dealt only with the figures for half the period covered therein.

The ATTORNEY-GENERAL—The prospectus does not always start in 1911.

Sir JOHN SIMON—In this heading it does.

*Re-examination continued*—I think you said you had heard of a trade cycle. Have you ever heard of the possible effect of war on a trade cycle?—I have not studied it.

Concerning the bonus declared by the Nelson companies, amounting to £200,000 in one case and £100,000 in the other, in 1927 you were asked questions concerning the difference between a bonus and a dividend. Were the dividends usually paid in cash?—They were. Cash did pass as the result of this bonus, but the cash that passed was repaid in taking up other shares.

All in the same week?—About a week.

Further cross-examined by Sir JOHN SIMON—Was the cash repaid to the same company?—Not all of it.

The prospectus gave particulars of the dividends paid between 1911 and 1927, after providing for all taxation, depreciation of the fleets, adding to the reserve, and so on. If the reserve referred to there was the published reserve fund, is it true that there was a great addition to the reserves between 1911 and 1927?—Yes.

How much was it?—The reserve fund was £1,180,000 and the insurance fund £1,051,755. Altogether this totalled £2,231,000.

In 1911 was there any substantial unpublished reserve?—There was not.

So that, whether it is the published or unpublished reserves, it is true to say that during those seventeen years (1911 to 1927) additions were made to reserves?—Yes.

Mr. JUSTICE WRIGHT—Nobody seems to know what the unpublished reserve was in the years 1921 to 1924.

The ATTORNEY-GENERAL—That will be dealt with later.

# The Royal Mail Case.

Arthur T. Cason

Further examined by the ATTORNEY-GENERAL—Having built up a reserve in 1911, if you had gone on at the rate you had been going on for the last few years, were you rapidly getting through it?—We had got through the unpublished reserves; we had exhausted them.

ALEXANDER HUGH M'GILL examined by Mr PRITT—I am chief accountant to the Pacific Steam Navigation Co., which is managed from Water Street, Liverpool. I have held that office since 1916. Since 1916, at any rate, the company has been one of the 100 per cent. subsidiaries of the R.M.S.P. From 1921 to 1927 Lord Kysant was chairman of the company. I produce statements showing the summarised profit and loss accounts of the company for those seven years. This statement shows the total deficit in each year. For example, the figure for 1921 was more than £735,000. Particulars are also given in the statement of the dividend paid for each year to the R.M.S.P. and the deficit of the Pacific Steam Navigation Company before that dividend was paid. In all the years referred to, with the exception of 1921, there was a trading profit, before deducting depreciation, but when depreciation is deducted the figures show a trading loss in every year. The depreciation figures are the amounts actually charged by the company. The basis of the depreciation charge was roughly 5 per cent, that is, assuming a life of twenty years, but I agree that the depreciation charge was in fact a little more generous in some years. In 1923, for example, there was a substantial excess.

Provision was made for depreciation in 1926 and 1927. Having regard to the actual value of the fleet at the end of 1925, and the written down value, was there any real need to apply depreciation in 1926 and 1927?—None whatever.

If the right way to get a true picture of 1926 and 1927 would be to cancel the debits for depreciation, there would be a real trading profit in each of those years—a figure of £144,000 odd in the one case and £196,000 odd in the other?—That is so.

I agree that in 1921 £100,000 was taken from the deferred repairs account—the account to which money was placed during the war to bear the cost of subsequent repairs which would ordinarily have been done earlier but for war conditions.

In 1926 and 1927 money was taken from taxation reserves. Were they free before they were taken?—As regards 1927, that was the final clearing up of the whole thing. I produce extracts from the P.S.N. Company minute-book, which record, among other things, that Lord Kysant (then Sir Owen Philipps) was appointed chairman in 1920, that shortly afterwards a special meeting was held at which he was reappointed, and that a year later it was resolved that he should no longer be subject to annual reappointment. There are other minutes year by year showing that the board approved of the dividends and the annual reports and statements, and that generally Lord Kysant was present and signed the minutes as chairman.

I produce a further statement relating to published reserves, also the reports of the directors of the company for the years 1926 and 1927.

## Evidence for Prosecution.

Alexander H. M'Gill

Cross-examined by SIR JOHN SIMON—Referring to the item in the summarised profit and loss accounts relating to the capital surplus on ships, does that represent profits made on certain ships which were sold for more than their book value?—Yes

As an accountant, do you say that when a ship is sold for more than its book value, the balance is distributable?—Yes.

Cross-examined by SIR PATRICK HASTINGS—Included in the profit and loss account for the year 1926, is there a sum of £148,000 from the obsolescence fund?—Yes.

Do you agree with the evidence given by Lord Plender that there came a point at which accountants might think it right to give shareholders some notice of these drawings?—Yes. The accountants of the Pacific Steam Navigation Company were the firm of Harwood Banner & Sons.

You would agree with me, would you not, that this firm is one of the biggest and best-known firms of accountants in the whole of Liverpool?—Yes, for many years.

Do you notice that the words in the profit and loss account for the year 1926 are these: "Balance for the year before providing for depreciation of fleet"?—Yes.

You notice that Messrs. Harwood Banner did not think it necessary at that time to give notification of the transfer from the obsolescence account?—Yes.

You notice they give a certificate that in their opinion the balance sheet is properly drawn up so as to exhibit a true state of the company's affairs?—Yes.

Do you agree that, strictly speaking, if the balance transferred from the obsolescence account was eliminated, there would be no balance?—Yes.

Do you also agree that it was stated that the auditors offered themselves for re-election?—Yes.

And do you notice, if you turn to the balance sheet for the next year, that the offer of Messrs. Harwood Banner was apparently accepted by the company?—Yes.

MR. JUSTICE WRIGHT—Messrs. Harwood Banner do not appear to have offered themselves for re-election for the year after that.

*Cross-examination continued*—Did the equally distinguished firm of Messrs. Peat become auditors in succession to Messrs. Harwood Banner?—Yes.

In 1927 was there again a transfer from this obsolescence account?—Yes.

A drawing upon the obsolescence account for the purposes of this account?—Yes.

Are the words on the statement for the year ending 31st December, 1927, "balance for the year before providing for the depreciation of fleet"?—Yes.

And again in that year did Messrs. Harwood Banner give a certificate in precisely the same form as they did for 1926?—Yes.

By the Court—Had this company any unpublished reserves?—Oh, yes, my lord.

# The Royal Mail Case.

Alexander H. M'Gill

Where do they appear on the general balance sheet? They must be there somewhere, or your accounts would not balance, would they?—Until they are definitely cleared up, some of them would appear in the debts owing by the company.

Re-examined by the ATTORNEY-GENERAL—Is it not correct that these matters would appear on the left-hand side of the sheet as debts owing by the company?—That is so, and if they appeared elsewhere they would come in as current voyages.

You were asked some questions about Messrs. Haimood Banner offering themselves for re-election. Do you see anything funny about them offering themselves for re-election?—No, it is quite the usual thing.

What was the number of the shareholders of the Pacific Steam Navigation Company?—One.

Who?—Royal Mail Steam Packet Company.

Who was the chairman?—Lord Kysant

And was Lord Kysant also chairman of the Royal Mail Steam Packet Company?—Yes.

And so far as you know did Lord Kysant know all the material facts?—Yes.

WALTER ANWYL WILLINGTON examined by Mr. PRITT—I am secretary and chief accountant of MacAndrews & Co., Ltd., one of the 100 per cent. subsidiaries of the Royal Mail Steam Packet Company. The registered office of the company is Royal Mail House, but it is managed from Liverpool. I produce the memorandum and articles of the company and a statement prepared from the books of account showing profit and loss and reserve accounts from 1918 to 1927. I have been secretary and chief accountant since 1924. Lord Kysant was chairman of the company from 1921 to 1927. I produce the statement which I have prepared from the books and accounts of the company showing the profit and loss and reserve accounts of the years 1918 to 1927. Among other documents I produce the profit and loss accounts and balance sheet for the year, signed by Lord Kysant as chairman, and containing an auditor's report in the usual form, signed by Messrs. Peat, &c.

Cross-examined by Sir JOHN SIMON—Just a question on Exhibit No. 82. Take the year 1920 and run your eye down that column. Two-thirds of the way down you come across a figure £180,745, labelled as depreciation extra over 5 per cent. Does that mean that in this shipping company in the year 1920, over and above depreciation, there was no less than £180,745 which otherwise might have gone as distributable profit, devoted to the further writing down of ships?—That is so.

So that from the year 1920 the fleet of this company stood in the books at a much lower figure?—Yes.

As a result of that, if you happen either to sell a ship or to lose a ship and claim insurance in respect of it, you will make a profit, because you get more than the book value of the ship?—It necessarily follows that if you sell a ship at more than the book value you do make a profit.

Run your eye down the column for 1922. Do you see a figure £84,021? Is that profit on the sale of ships?—Yes.

## Evidence for Prosecution.

Walter A. Willington

On how many ships?—Two ships.

Looking at the details for 1920, I notice that the profit on voyages had gone up by over £100,000 and I suggest that that was a very good year for the company?—I agree.

One way of dealing with it would have been to say “Here is a very large additional gain; let us distribute it.” The other way is to say “Let us put it aside, because there may be a time when we shall be very glad to use it”?—Yes.

Do you agree that the company had pursued a very conservative policy of not distributing all gains?—Yes

I don't know whether conservatism is a good thing in finance, but there seems to have been a good deal of conservatism about this company?—This company certainly has been very conservative

And Lord Kysant was chairman of the company?—Yes

Re-examined by Mr. PRITT—Is it not correct that in 1927 the sum written off for depreciation was only £19,000?—That is so.

If the depreciation, in fact, of the vessels was proceeding as fast in 1927 as it was in 1926, the actual diminution in value would, of course, be approximately the same?—That company had depreciated at approximately 5 per cent. per annum.

Is it not a fact that the depreciation of 1927 was provided partly out of the receipts or earnings of 1927 and partly out of the receipts or earnings or prudent provision of earlier years?—Yes.

THOMAS SMITH examined by Mr. FULTON—I am chief accountant of David M'Iver & Co., Ltd., of 21 James Street, Liverpool. I have prepared the accounts of that company since 1918, and during that period Lord Kysant has been chairman. I produce an exhibit which shows, in summarised form, the profit and loss account of the company for the period 1918 to 1927

I will not trouble to deal with the years before 1921. Does the document before you show a deficit for the year 1921 of £16,840?—Yes.

And in that year does it show that the company brought from general reserves account £25,000?—Yes.

In 1922 does it show that there was a deficit of £7418?—Yes.

And that the company again brought into account from general reserves £25,000?—Yes.

In 1923 was there a surplus of £2858?—Yes.

And did the company bring into account for the purpose of paying its ordinary dividend that year, from taxation reserve, some £20,000?—Yes.

In 1924 was there a surplus of £22,852?—Yes.

And nothing was brought in that year from any reserve?—No.

In 1925 was there a deficit of £29,458?—Yes.

And did the company bring in from taxation reserve £30,000 in that year?—Yes

In 1926 there was a deficit of £21,431?—Yes.

And did the company bring in from taxation reserve £16,273?—Yes.

# The Royal Mail Case.

Thomas Smith

In 1927 was there a surplus, and nothing appears to have been brought in from reserves?—Yes.

Is it not correct that over a number of years, beginning in 1919, the accounts of the company were put before the board and considered and approved by them?—I have not extracts going so far back as 1919. My extracts begin on 8th February, 1921.

Lord Kysant, as I understand it, was chairman of the company during that period, but in fact he was not present at any of the meetings except the first one of 8th February, 1921?—That would be so according to the record of attendance.

Do you produce a further exhibit which contains the directors' report, balance sheet, and profit and loss accounts for the years 1926 and 1927?—Not the directors' report: it contains the accountants' report.

It appears in the depositions as the directors' report. What does it in fact contain?—The accountants' report.

Mr. JUSTICE WRIGHT—It seems to be countersigned by two directors.

Cross-examined by Sir JOHN SIMON—You have been good enough to hand down to me the minute-book, and I am just looking at the occasions when accounts were considered. Except on the one occasion when Lord Kysant was present, and took the chair, as I make out, the gentleman who usually took the chair was Mr. Charles Livingstone?—Yes.

A gentleman of high reputation in shipping circles?—Yes.

And the company is called David M'Iver & Co., Ltd.?—Yes.

It bears the name of one of the best-known and most respected shipping authorities in that part of the world?—Yes.

And Messrs. Harwood Banner were the accountants?—Yes.

Should I be right in suggesting that the company was conducted on very conservative lines?—Yes.

I am using the word in a commendatory sense Depreciation at 5 per cent.?—Not invariably, sometimes at 4 per cent.

CYRIL GORDON MATTHEWS examined by the ATTORNEY-GENERAL—I am assistant accountant of the Royal Mail Steam Packet Company, and I have been employed in the accountancy department since 1918. From 1921 onwards I have been dealing largely with the taxation matters, both in connection with the R.M.S.P. Company and the Meat Transport. I had the task of dealing with excess profits duty and income tax. A colleague and I have prepared a statement showing the position of the item or items on the balance sheet relating to sundry reserves. I have consulted the general balance sheet for the year ended 31st December, 1921. The table shows a total of sundry balances amounting to £6,279,000. Looking at the figures for the year 1922, I agree that sundry balances there appear at £5,042,000. Dealing with the figures for 1921, the excess profits duty was put at £816,527, income tax at £762,431, deferred repairs £425,146, corporation profits reserve £34,420, war contingency reserve £45,050, exchange reserve £54,563, premises reserve £30,000, and Government charters reserve at £63,937. As regards the following year, the exchange reserve had gone down to £34,000 and the premises reserve

## Evidence for Prosecution.

Cyril G. Matthews

remained at £30,000. The item for Government charges had become £3900.

Just run on, will you, to the year 1925. Do you see there the excess profits duty figure as at 31st December, 1925, was £390,277?—Yes.

And on the corresponding date of the next year, 1926, the excess profits duty figure stood at £110,277?—Yes.

You will observe that there is a difference of £280,000?—Yes.

If I look to see what happened in the course of the year 1926, I shall find, shall I not, that £550,000 went out of the reserves to profit and loss account?—Yes.

Just explain to the jury, if you will, why it is that starting with £390,000 I find in the course of the year 1926 £550,003 goes out, and at the end of the year 1926 you have still got £100,000. Just explain in your own words?—We had £330,000 in cash from the revenue during the year.

By Sir JOHN SIMON—Is that received in the year 1926?—Yes.

*Examination continued*—Let us start this way, if you will. The year 1925 concludes, and there is a balance of £390,000 standing to the credit of the excess profits duty reserve?—Yes.

In the course of the year 1926 that reserve is augmented in certain ways and drawn upon in certain ways?—Yes.

It is augmented because there are in the year 1926 payments from the Inland Revenue, or repayments, of £330,000?—Yes.

So I start my sum by adding £330,000 to £390,000, which is £720,000?—Yes.

This sum is depleted in the course of the year 1926 to the extent of £550,000, which is taken to the credit of profit and loss account?—Yes.

That leaves £170,000?—Yes.

And £60,000 is attributed to one of the subsidiaries?—Yes.

And that leaves £110,000?—Yes.

By looking at this table, therefore, we can see on the various dates, as we pass the mileposts, exactly what there was credited to that account and for each year what was brought in, and then we shall be able to check it on the mileposts. That is the position, is it?—Yes.

By the COURT—There was a payment of £330,000. Was that a refund of something that had been paid over in previous years in respect of excess profits duty?—Yes, my lord.

*Examination continued*—Now, as to the building up of the fund—never mind from where it was obtained—what was the last payment that was made to the credit of the excess profits duty reserve?—£125,000. That was credited to the account in 1921.

Is that the figure which I find here as a special debit in the year 1921?—Yes.

Sir JOHN SIMON—You used the expression that it was a repayment from outside. It is a transfer.

The WITNESS—A book entry.

The ATTORNEY-GENERAL—That is a very complicated subject. I want



# The Royal Mail Case.

Cyril G. Matthews

to consider for a moment the building up of the fund excluding payments to the Inland Revenue.

Sir JOHN SIMON—I thought you asked what was the first year in which a payment was made, and he thought you did not mean “Payments from the Revenue.” It is a transfer, of course, from another ledger.

The WITNESS—That is so.

*Examination continued*—I meant to ask the last date when any credit or transfer was made which went to the building up by augmentation of this fund, and the answer you gave was that £125,000 was credited or transferred in the year 1921?—Yes.

When that sum had been paid, what was the sum total of the credits which had been placed to the credit of this fund?—£2,260,600.

Does Exhibit No. 56 show your figure of £2,260,600?—Yes. These are not payments in a sense of payments to outside people at all, but the various credits or transfers to that fund from 1915 to 1921.

For the purpose of excess profits duty you had to group together the parent company and the various children?—Yes.

I want you, if you can, to allocate such part of the repayment as represents the liability of the parent, the R.M.S.P., and how much was paid to the Revenue, taking it for the whole period—the amount really paid to the Revenue out of the £2,200,000?—£1,179,287.

If I subtract that figure from the total of the fund, I get £1,081,313?—Yes

May I take it then, subject to a more careful survey of these figures, that the total of this fund is £2,200,000 odd? £1,100,000 has been actually paid over to Inland Revenue, and £1,100,000 represents credits and transfers standing to the credit of the fund?—Yes. The last instalment was paid during 1919.

Let us deal first of all with the £1,100,000 which was never paid over, but which stands as a credit to the fund. Was £300,000 of that credit utilised and put to the investment and depreciation account?—Yes, in 1921.

That means to say, in round figures, that the part not paid over has now been reduced to £800,000?—Yes.

And how was the rest of that £800,000 used?—£800,000 is rather a nebulous sum. It just happened. In the end it was taken to profit and loss.

We will check it out in detail year by year. Now of the £1,100,000 which had been paid over, the last part of it being paid over in 1919, what part of that was repaid—how much of it?—Over £800,000.

Now can you give me the dates on which these repayments were made?—I am not separating these payments for the parent company from the repayments for the subsidiary companies, the repayments for the whole group being £1,370,000. In February, 1923, the amount was £500,000; in January, 1924, £300,000; in June, 1924, £250,000; in April, 1926, £73,133; in July, 1926, £50,000; and later in July, 1926, £180,000; and in May, 1927, a final payment of £20,067.

## Evidence for Prosecution.

Cyril G. Matthews

By the COURT—What is the total of those figures?—£1,373,200.

*Examination continued*—Of which, I gather, £800,000 represents the parent company repayments?—Yes.

Sir JOHN SIMON—I thought this gentleman had given a number of figures of repayments representing a sum of roughly £1,370,000. Is that right?

The WITNESS—Yes.

Sir JOHN SIMON—And I thought the earlier figure which I indicated I would agree was E.P.D. £1,100,000?

The WITNESS—Yes, R.M.S.P. only, that was.

Sir JOHN SIMON—If these two figures are both right, the result on balance of the whole thing would be that the Revenue authorities appear to pay rather generously.

*Examination continued*—You have written out the portion of the repayment which should be allocated to the parent company?—I can tell you how much of these repayments were kept on account of the parent company. Of the £500,000 in 1923 we kept £250,000. Of the £550,000 in 1924 we paid away £160,000 and we kept £390,000. In 1926 payments were made rather difficult, for when the Revenue repaid this money they did not say what they were repaying, because income tax and excess profits duty were very mixed. So they called this £330,000 of excess profits duty "income tax." In May, 1927, we had a very complicated settlement with the subsidiary company, and I am afraid I cannot say exactly how much of the cash we kept. We took what was left as due to us, only about £20,000. The money we had kept was only by guessed figures, and when we came to the end of the period we found we had kept back too much from the subsidiaries or given them too much, and therefore we adjusted these figures to arrive at the right amount. We kept back cash from 1927, and we paid cash over to subsidiary companies because the payment we had kept was £910,000, which was too much, and so we made payments to the subsidiary companies of the £20,000 which we received in cash.

By Sir PATRICK HASTINGS—Am I not right in saying that for that last year out of the constructive repayments you took for the parent company a constructive repayment of £551,000? Look at that letter of 18th May, 1927, from the Inland Revenue—is it not clear from that that the R.M.S.P. took from the last three figures quoted there their share of £551,000?—I have not the figure, but a constructive payment would not be a payment in cash.

I appreciate that, but that was the amount they took?—I do not recognise that figure.

*Examination continued*—Again this is a very complicated matter, and these constructive repayments come to nearly another million. For the moment I prefer to consider cash. As to the £1,300,000, I have practically got the facts about that, have I?—Yes.

Just look at this table which I have introduced, and we will just see year by year what happens to the excess profits duty. I think this will make it plain. I start you at the year 1921, and I select that year

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Cyril G. Matthews

because that is the last time this fund has been augmented by a credit?—Yes.

£866,527 is the amount of it there?—Yes.

Next year, £716,527?—Yes.

Is that a perfectly simple utilisation of a credit of £100,000 in the course of the year 1922?—To profit and loss.

At the end of the year 1923 the £716,000 has grown to £866,000?—Yes.

In the course of the year 1923 £100,000 has been taken out?—Yes.

Will you tell me what it is that has come in, and from what quarters, to make the £716,000 up to £866,000, notwithstanding the payment of £100,000. In the next year that £866,000 has gone down to £690,000, and in the course of the same year £330,000 has been taken to the credit of the profit and loss account. So I should expect the £866,000 to be down to £536,000, so there must have been a credit which has brought the £536,000 up to the larger amount?—We started with £866,000, we had £550,000 in cash, which brought it up to £1,316,000; then we paid away to subsidiaries £160,000, we transferred to income tax reserve £235,250, because we had to pay income tax on the excess profits duty repayments. Then, taking £330,000 to profit and loss, that leaves a balance of £690,000. We added £550,000 which was received in cash and then deducted £160,000 paid in cash to subsidiaries. So £236,250 was transferred to income tax reserve. 1927 was the first year in which the exact figure of repayments was known.

Did the Revenue ask you to repay to them what they had paid you?—No, but they refused to pay us any more.

By the Court—There was a payment for 1919, I gather?—That was the last payment by the R.M.S.P.

*Examination continued*—By 29th March, 1923, had the liability in respect of the six companies been decided?—The liability for 1919 was £726,000. By October, 1923, by writing off allowances, the figure had been agreed at £3,300,000.

And by October, 1923, was it possible to estimate what the final result would be?—An estimate was made in December.

The income tax reserve started in 1921 with £762,000 and by 1922 it was £529,000?—Yes. That money would chiefly go in cash to the Revenue. The first year in which the fund was used was in 1923, and at the end of the year 1922 there was £529,000 standing to the credit of that account. In the course of 1923 £450,000 went out to profit and loss account. With regard to the corporation profit tax reserve, that was built up originally in 1920, and it had a transfer in the course of the year 1927 to its credit.

The history of the fund is that it was built up by a special debit in 1920 of £34,000, and there was a special credit of £40,000 in 1924, and the fund was augmented as part of the general settlement with the Pacific?—Yes. With regard to the "balance proof" for the purposes of income tax reserve, that was prepared in March or April after the accounts were closed. I also produce the accounts relating to the

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following year. That is the history, so far as I have been able to tell, in relation to the building up of the taxation reserve.

If you take the year 1921, is 2½ million the sum total of the taxation reserve, and do you find that at the end of the year 1927 the sum total is £329,000?—Yes.

You have had very substantial repayments in respect of E.P.D.?—Yes.

And they have been put in to swell those reserves?—Yes.

And at the end of 1927, had you, so far as you could see, substantially come to the end of any possible augmentation of your taxation reserve?—Yes.

Cross-examined by SIR JOHN SIMON—There is one figure at the beginning which I indicated I did not follow. Perhaps you will look it up and tell me about it in the morning. You gave us a figure of £2,260,000 as the total amount which in the seven years 1915 to 1921 the company had provided from profits to the credit of E.P.D. reserve. The figure which I don't follow is the figure you next name, where you said that the actual liability in the end of E.P.D. was £1,179,287?—No. I think you misunderstood. That was the amount which had been paid on account. It bore no exact relation to the liability.

Is the £1,179,287 the cash that was paid by the R.M.S.P. on E.P.D. account to the Revenue?—Yes.

The actual liability for E.P.D., however discharged, was agreed in 1927 at £1,769,122?—Is that before deducting the allowances?

My figure, as supplied to me, is this. That during the seven years 1915 to 1921 the R.M.S.P. provided from profits to the credit of E.P.D. reserve £2,260,000. The actual liability is finally agreed in 1927 at £1,769,122, without deducting any obsolescence allowance. The obsolescence allowance was finally agreed in 1926, and I ask you, was the figure agreed at £1,190,544, and the repairs allowance agreed in 1926 for the R.M.S.P. for £238,161?—Yes.

If we add that last figure to the £1,190,544 obsolescence allowance, they come to £1,428,705, the sum total that the Government in the end allowed back to the R.M.S.P. on obsolescence account?—Yes.

The Court adjourned.

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Fourth Day—Thursday, 23rd July, 1931.

## Evidence for the Prosecution—Continued.

CYRIL GORDON MATTHEWS, further cross-examined by Sir JOHN SIMON—You see what has been done in Exhibits Nos. 93 and 95. Merely to extract some figures. They really are the figures which, taken all together, produce by addition and subtraction what is termed the right-hand side of the profit and loss account in 1926—the sum of £439,212—and in the same way the other document you have shows the figure for 1927 at £697,456. Is that so?—Yes.

So far as the income tax figure, which is the second figure on both pages, £175,000 in the one case and £120,000 in the other, is concerned, we have, through other witnesses, ascertained that those amounts became available in the year 1926 or 1927, and were promptly transferred to profit and loss. Is that so?—Yes.

They do not come out of old reserves at all?—No.

With regard to the excess profits figures of £550,000 in 1926 and £232,788 in 1927, would it be fair to say that those figures were figures which were not properly transferable to profit and loss account until the year in which they occurred, in 1927?—The situation was that there were three different disputes in settling up the E.P.D. First, the Crown's claim against the company for E.P.D., and that was a claim which the company should pay to the Crown. Then there was a second dispute as to what would be recognised as the obsolescence allowance, which was a question as to how much the Crown should pay to the company. And, thirdly, there would be the deferred repairs allowance, which again was a thing which was to be paid or allowed by the Crown to the company.

Am I right in saying that, taking those three things together, and to arrive at the ultimate settlement, one has to wait until the year 1927?—Yes.

That is the year in which the sum total was fixed?—Yes.

In the end it turned out, when all was done, that after they had been properly fixed the Crown was to receive certain money from the company, and there was subtracted the two amounts, and the ultimate result was that there was £340,417 net, which was the liability for the whole period to the Crown?—Yes.

And the date when the final agreement was reached was 18th May, 1927?—Yes.

The £340,417 would be paid and discharged out of the earnings of the company?—Yes.

In fact E.P.D. is a duty upon profits?—It is part of the profits paid over to the Revenue.

In 1927 the amount of balance on profits that the Crown would want was £340,000. Am I right in saying that the company from first to last

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provided in its accounts for the claim which the Crown might make for excess profits duty, £2,260,000?—Yes.

Without making allowances for the other way?—Yes.

So if you take the seven years, the company thought it prudent from time to time to secure that, if it was called upon to pay excess profits duty, it would have the money for the purpose?—Yes.

Was that a perfectly prudent and perfectly proper thing to do?—Yes

Although the net balance which had to be found was only £340,000, you told me yesterday that so far as the claim of the Crown against the company was concerned the claim turned out in the end to be £1,769,000?—Yes

It was safe to bring the money into the profit and loss account. It remained undistributable profit?—Yes.

And as the years went on, 1923, 1924, 1925, 1926, and 1927, we find that these large sums of hitherto undistributed profit are brought back year after year into the profit and loss account and become distributable profit?—Yes

There is no doubt that it is profit?—No.

In 1927 I notice that the excess profit figure is not a round figure, but a figure of £232,788?—Yes.

Was that sum ascertained to be the amount, and the exact amount, which should be taken into the profit and loss account in that year as soon as you had settled up between the R.M.S.P. and its subsidiaries?—Yes.

The other things that happened in this other year 1927 were: first of all, there was a final receipt from the revenue of £20,000; secondly, there was an agreement finally reached in 1927 which fixed the figure; and, thirdly, there was a very complicated thing settled up or adjusted between the R.M.S.P. and its 100 per cent. subsidiaries?—Yes.

As soon as ever that was done, was this £232,000 odd transferred to profit and loss account?—Yes.

Is there any doubt that that item is an item which was properly transferred in that year?—There was no doubt at all. We could not have transferred it before.

You would not take the view that this £232,788 was lying somewhere as an old reserve of long ago, and in 1927 suddenly it occurred to you to turn it into the profit and loss account?—No.

It was connected with the events of 1927 and had been earned profits all the time. It could not be put into the profit and loss account until that moment?—That is so.

You will have noticed that the Crown have made an exhibit of a document called a balance proof in the income tax account. Was there also a balance proof of excess profits duty account—one of the documents that would be under your charge?—Yes.

If you look into the excess profits ledger you will find that £390,277 of profits of the company was being kept as balance there in view of possible claims for E.P.D.?—Yes.

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Was that in fact the position at the beginning of 1926?—Yes.

Does this balance proof of E.P.D. of 31st December, 1925, help one to see what at the time was thought might at any rate be the claims against you?—Yes.

Therefore it gives one a glimpse as to what was the view that the company was taking at that moment, the beginning of 1926, of what its liability might turn out to be?—Yes.

And the view that was being taken in the accountancy department?—Yes

If I understand this document rightly, it seems to show that so far as was estimated then, this £390,377 was a balance which ought to be kept and not immediately distributed?—Yes

Because when I look on the other side, you will see, it is only an estimate, that there was an estimate of a total E.P.D. liability less paid on account of £472,000, and that is a bigger amount than the £390,000. Lower down, there is an estimate of the obsolescence allowance, and that had not been settled, and some had not been paid?—That is so.

Is it in your view a prudent matter that you should not anticipate payments that you hope to get from the Government before you get them?—Certainly.

Does this balance proof as at 31st December, 1925, show that at the beginning of the year 1926 the then balance, £390,277, ought for the time to be retained?—It would be prudent to retain it

Let us look at the ledger which records what happened to the £390,277 during the year 1926. That is a figure which could not have been distributed until 1927?—Yes

Down to that moment it was properly held to meet possible claims?—Yes.

What happened in that year was this: some six months later, in July in the year 1926, the Government with generosity paid £330,000 in cash to the R.M.S.P. Company?—Yes.

Being a payment on account of the reduction of what was the liability in view of obsolescence account and other things?—Yes.

It means that at one time the Crown had taken up the position that £330,000 of profit made by the R.M.S.P. belonged to the Crown, and now they said: "We have £330,000 of your profit which we ought to give you back, and here it is"—Yes.

By the COURT—In fact, it was a repayment of the amount before the obsolescence account had been ascertained?—Yes.

Sir JOHN SIMON—It is in the nature of profits of the company all the time.

*Cross-examination continued*—The next thing is that there is £330,000 received in July, 1926, from the Revenue by the R.M.S.P., but look on the other side of the account. Was £60,000 of that passed by your department to the subsidiaries?—Yes.

When these E.P.D. discussions and settlement took place between the Revenue and the R.M.S.P., the R.M.S.P. represented the subsidiaries?—Yes.

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Was a part of the money returned to the subsidiaries a sum of £60,000 which the R.M.S.P. thought necessary to transfer?—Yes.

That leaves you with £270,000?—Yes.

If I add the £270,000 to the £390,000 with which the year began, I shall get over £600,000 altogether, and in December, 1926, there was a transfer to profit and loss of £550,000?—Yes.

And the balance with which the next year begins is reduced to £110,000?—Yes.

Does that mean this: that in view of the fact that there had been in 1926 a final settlement of the obsolescence and the deferred repairs, notwithstanding the fact that it was not until 1927 that there was a final settlement of E.P.D., it appeared reasonable to reduce the balance of £390,000 to £110,000?—The air was much clearer at that time.

And it was possible to cut the thing a little closer?—Yes

It is, of course, profit?—Yes.

The excess profits duty credits were £550,000?—Yes.

You would not take the view that that was part of some antiquated reserve of years and years?—No, I cannot say that the £550,000 was a definite ascertained figure that arose in 1926.

You have to do what is prudent?—Yes.

In the year 1926 had there been, apart from the receipt of the £330,000, what has been called a constructive repayment?—Yes

What was the amount of that which the company received in the year 1926?—The R.M.S.P. got £551,022.

Does it occur to you that the company having received £551,022, £550,000 transferred from the profit and loss account at the same time, in the same year, was a perfectly proper thing to do?—Yes, the exactness of the figure was a coincidence.

By the Court—Part of the money due to the R.M.S.P. for obsolescence was set off as money due by the R.M.S.P. for E.P.D. which had never been paid.

*Cross-examination continued*—If we take a survey now of what was happening between 1921 and 1927, this seems to me to be the story. In 1921 there was no part of any excess profits duty earmarked, but £300,000 of the provision was used to write down investments?—Yes.

That means that you are really improving your position, but that you are not paying any money away, and you have it there in case of need?—Yes

And in 1921 there was no transfer from the E.P.D. to profit and loss account, but £300,000 was used to write down investments?—Yes.

In 1922 you got £100,000 transferred to profit and loss?—Yes.

In 1923 you began to get actual repayments from the Revenue?—Yes.

And in that year the amount that was received is, so far as the Royal Mail is concerned, £250,000?—Yes.

And in 1923 there was another £100,000 transferred to profit and loss?—Yes.

In 1924 the Royal Mail received £390,000 not from the Revenue?—Yes.



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And in the same year £330,000 was credited to profit and loss?—Yes.

In 1925 no cash was actually received, but the deferred repairs claim was finally settled in January, 1926?—Yes.

The accounts for the year 1925 were not settled on 31st December?—No, they were settled in April and May.

And when the time came to settle the amounts, you knew that the deferred repairs claim was finally settled?—Yes.

And in the accounts of 1925 did you credit £300,000 to profit and loss?—Yes.

Taking rather more out than before?—Yes.

Did you consider that was justified because the position was becoming more clarified?—Yes.

In 1926 the company received £270,000. There was this constructive repayment, and £550,000 was transferred to profit and loss account?—Yes.

And was it prudent to do so?—Yes.

They were just as much profits?—Yes.

It was a question as to whether the Crown or the company should have them?—Yes.

In 1927 you get a complete settlement in the course of the year of everything?—Yes.

Am I not right that the ascertainment of the final sum which settled this up occurred, after 11th May, 1927, which was the date when the balance sheet of 1926 was signed?—That is so.

Then could it have been dealt with until the next year?—No.

And was it dealt with in 1927?—Yes.

Mr. JUSTICE WRIGHT—I want to know how the item of £110,000 was swollen to £232,000. The company started with a balance of £110,000, and finished with a balance of £232,000. Something must have caused the original balance to be increased.

Sir JOHN SIMON—The simplest way to get at the facts is to call attention to the “ sundries ” item which appears at £1,198,000, although on the other side of the account there is another item of more than £1,000,000.

*Cross-examination continued*—Explain what was included in the “ sundries ” item?—In that connection “ sundries ” did not mean what it usually meant. It there meant that a number of accounts were concerned in one item. The position of the subsidiary companies was that there was, apart from the adjustments, and apart from any income tax reserve, a collection of accounts which related to E.P.D. There was a cash collection of £40,000. There was a sum of £120,000 standing in other accounts in the company's ledgers, and it was collected into the E.P.D. item. There was nothing outside, except for £40,000, which was paid to the Nelson Company. The Revenue had overpaid the R.M.S.P. for the income tax refund. When the Revenue ascertained that too much income tax was being refunded they adjusted the E.P.D. amount which was owing to the company.

By the COURT—They actually paid in that year £20,000. The

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company started with £110,000 to the good and got about £100,000 more by settling up the various accounts, and bringing them back to the E.P.D. account, where they ought to be?—Yes.

*Cross-examination continued*—It is easy to deal with millions as a phrase, but was this settling up between the subsidiaries and the R.M.S.P. a very elaborate matter, involving many cross-claims?—Yes.

Was it possible to carry it through and complete it until there had been a final settlement between the Revenue and the R.M.S.P.?—It was not possible.

That was only possible in 1927, and therefore the settlement with the subsidiaries could not be until then. Until you had settled with the subsidiaries and cleared the books, would it have been proper to transfer from E.P.D. and distribute all of it, or leave something as a provision for E.P.D.?—No, it would not.

By the COURT—It appears to be a payment to profit and loss account, which was properly made in 1927 and could not have been made before?—That is so.

*Cross-examination continued*—It is not in the least degree of the character of an old free reserve?—No.

So much for E.P.D. I see that in the year 1927 there is a corporation profits tax transfer. Which was the year when the corporation profits tax was imposed?—I think it was 1920

Which was the year in which it was brought to an end?—30th June, 1924.

Notwithstanding that this unpleasant impost came to an end by law in June, 1924, did discussions between the taxpayers and the Revenue as to how much they owed under it continue for some time?—Yes.

And in the case of the R.M.S.P. did it continue until the year 1926 or the year 1927?—1926, I believe.

Down to that time any reserve that you have to make to meet corporation profits tax claims was something which you must in prudence keep?—We only kept just over £1000 over those years, because we knew pretty well in 1924 that there would be no liability.

What was the corporation profits tax of £32,000 in 1927?—That was an amount except for the £1420 we had kept to keep the account open—the rest of it was collected from the Nelson Line in the final settlement of E.P.D.

It was collected in the year 1927?—Yes.

With regard to the corporation profits tax of £32,905, is it correct to say that that was not an old free reserve, but was made up of a sum which you got in 1927 in connection with the settlement of E.P.D. with the Nelson Line?—Yes.

Would it have been possible to have used this amount of £32,905 according to ordinary prudent business in advance of the year 1927?—No. I could not recollect whether we could have collected it before, but we did not.

There had been the sale of premises, both in London and Barbadoes,

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which was finally settled in 1926 or 1927. When that money became available, was it transferred to the profit and loss account?—That is so.

There was also a ship which was sold. One of the units of the fleet had been standing in the books of the company as though it was worth  $x$  pounds. It was sold for  $x$  pounds, plus  $y$  pounds, and  $y$  pounds was the profit?—That is the correct description of the matter, and the  $y$  pounds represented the extra depreciation which had been written off the vessel.

Profits had been used to write it down?—Yes.

When you found it was worth more, you ascertained that  $y$  pounds were realised and available for distribution as profits?—Yes.

And £6093, is that figure in 1926?—Yes.

In 1927, out of a large total of more than £1,000,000, there were sundry trading items passed or transferred. There was a composite figure of £17,000?—It included butter freights of about £13,000 which had accumulated.

There was the Government charter's reserve?—The Government charter's reserve had been gradually liquidated, and there was a small amount left over at the end. The only thing we could do with it was to bring it back into profit and loss.

Re-examined by Mr. PRITT—In various years, and we are only dealing with two strictly, a sum of money was transferred from E.P.D. reserve to profit and loss account?—Yes.

Who decides the precise figure to be transferred? Do you know, or does the decision merely get passed on to you?—As to how much is to be taken out, I suggest the figure.

You suggest the figure to Mr. Cason, and you receive from Mr. Cason, either with or without delay, a decision in the matter?—Yes.

Sometimes your suggestions would be adopted?—More or less.

I call your attention to the E.P.D. reserve account for December, 1925. On one side is the item "Balance per ledger, £390,000," and on the other side is "E.P.D. liability, less payment on account, £472,000." That was the liability anticipated at the time. There was also, in the same account, an item of £640,000, which was described as "Surplus reserve for liability"?—I made the entry in question, and it was correct as far as could be estimated.

On the best view of the matter which could be formed in December, 1925, that figure was regarded as surplus reserves?—Yes, but you should take into consideration the fact that there are deductions from it.

What deductions?—The transfers to profit and loss in 1922, 1923, 1924, and 1925.

Sir JOHN SIMON—I must have misread the account. I thought the account dealt with the E.P.D. liability, and that there was the obsolescence allowance. I understood that the figures, so far as obsolescence was concerned, were only estimates.

The WITNESS—The company thought that the total liability was £1,620,410, and they had reserved £2,260,000, or a difference of over £600,000.

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*Re-examination continued*—You thought at that time your reserves were in excess of your total expected liability by the sum of £640,000?—Yes.

The full position is this: you expected at that time that you would receive £1,608,000 in respect of obsolescence allowance, and that you would have the benefit or credit of £1,608,000 for obsolescence allowance?—Yes.

If that is added to the £640,000, you get just over £2,250,000. You pointed out that £1,366,000 of that had already been used to benefit other accounts, including the profit and loss account?—Yes.

One view of the figures was that there was a spare reserve of £640,000. Another view of the figures was that there was a credit of £886,000?—Yes. The obsolescence allowance did not include any amounts which would be paid to subsidiaries. Part of the obsolescence allowance was in due course paid over to the subsidiaries.

In addition to the £410,000 already paid?—Yes.

What was the amount ultimately paid?—Between £400,000 and £500,000 more.

You gave a round figure of £400,000; is that in addition to the £410,000 you see in the account?—Yes. The amount was actually £430,000.

By the COURT—They got in all £840,000 out of the £2,000,000?—Yes.

*Re-examination continued*—The position at the end of 1925 as between the company and the Revenue was very similar to that which existed between the company and the Revenue at the end of 1923?—We had a clearer idea of what the liability was to be. There was no very great difference.

Neither side had paid anything to the other in 1924 or 1925?—There was a payment in 1924.

It was £550,000?—Yes.

Had your prophecies and expectations at the end of 1923 proved to be substantially correct at the end of 1925?—We were fearing a liability of £100,000 more at that time.

Not a further payment, as you had overpaid?—Yes.

After 1923 there was no likelihood of the company having to put its hand into its pocket?—No very great likelihood. In 1925 the estimate was £100,000 more than the estimate of 1923.

In 1926 we know that the actual transfer to profit and loss account was £550,000?—Yes.

We know that there were payments in cash of £330,000 and constructive payments of £551,000?—Yes.

In substance, was that what you expected, or more or less than you expected, on the general position of your negotiations with the Revenue? Did you expect to get as much as £330,000 in cash and £550,000 in allowances?—I think we expected it. We were in constant touch with the people who dealt with the figures and the Revenue, and knew from day to day how things progressed.

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You received neither an unexpected windfall nor a stunning blow?—Neither

By July, 1926, payments, actual and constructive, were made?—Yes

Did you suggest in 1926 the figure to be taken from the E.P.D. reserve, and put into the profit and loss account?—Yes

When did you make the suggestion?—When the accounts were closed, about March, 1927.

What did you suggest?—£350,000.

Did you know then that £350,000 had been provisionally suggested in September, 1926?—Very possibly it was in September, 1926, I suggested it. When Mr. Cason made out the estimated profit and loss account, the suggestion was made.

That was in the autumn of 1926. Would £350,000 have been a wrong figure?—No, it would have left us a wider margin.

£550,000, was that a right or a wrong figure?—That was a right figure, but it was as much as I should like to take.

Do you know that Lord Kylsant had directed that the figure should be £550,000?—I was asked whether £200,000 more could be spared and I said it could.

If you had been asked whether another £200,000 could have been spared, what would you have said then?—I do not know what I should have said then.

All these sums of money have been derived from profit?—Yes.

Not from profit earned in 1925, 1926, or 1927?—No.

By the Court—They were earned before 1920, I suppose?—Yes.

*Re-examination continued*—The last transfer to the reserve was?—1921.

Further cross-examined by Sir JOHN SIMON—No doubt it was known to you that by the provisions of the Income Tax Act, where any person has paid E.P.D. the amount so paid shall be allowed as a deduction in computing the profits of the year for income tax purposes?—Yes.

But where any person, or company, has received payment of any amount previously paid as E.P.D. the amount so repaid shall be treated as profit for the year in which the repayment is received?—Yes.

By the Court—Were they charged with income tax?—Yes. All the cash repayments and the constructive repayments were brought in as profits for income tax for the year in which they were repaid. Constructive repayments were brought in during 1926.

*Further cross-examination continued*—What is received back has to be treated as profit for the year in which the repayment is received?—Yes.

When income tax is paid on that, *pro tanto*, the figure of assessment would be enlarged?—Yes.

Whether it ultimately produces a net profit or not for the year depends upon other things?—Yes.

By the Court—It would simply go into the general balance. It is not a subject of a separate assessment?—No, it goes into the ordinary assessment.

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SIR JOHN SIMON—It is treated as an element of profit in the year.

MR. JUSTICE WRIGHT—And therefore brought in with the other profit. Even after allowing for it, however, there might in some cases be no balance of profit left.

SIR JOHN SIMON—I agree. There was a great deal of controversy regarding that particular matter before it was finally settled. Section 39 of the Finance Act of 1921 provided. “Notwithstanding anything to the contrary in the principal Act, repayments and adjustments of E.P.D. may be obtained and made and additional assessments to the E.P.D. in respect of E.P.D. in any accounting period unless and until Parliament otherwise determines.” After 1921, although E.P.D. had come to an end, the Legislature expressly said that the liability to assessment or additional assessment in respect of any accounting period was to go on unless and until Parliament determined. The year in which Parliament so determined was 1926. The actual provision in that year was that what had been settled should be treated as final, unless the Revenue gave notice that there was an outstanding dispute which could be left over.

THE WITNESS—In 1926 the E.P.D. liability of the R.M.S.P. was still undetermined. It was not finally determined until 1930, although the amount outstanding up to that time was small.

BY THE COURT—Was that why you kept £5000 aside?—In 1930 we had a further refund of £1300. That was early in 1930, and that was the settlement.

MR. JUSTICE WRIGHT—When had the special notice required under the Act of 1926 to be given?

SIR JOHN SIMON—I think it was called a notice of “non-determination.” If the Revenue thought they had something they could usefully dispute, they had to give notice of non-determination, and in that way could keep the matter alive.

MR. JUSTICE WRIGHT—I suppose a time was fixed during which they could give that notice?

THE WITNESS—Notice was given to us in September, 1926.

SIR JOHN SIMON—The wheels of the Revenue grind exceedingly small, and sometimes slowly. (*To witness*) I gather that notice of undetermined liability was served on the R.M.S.P., and that it was not finally settled until 1930?—That is so.

It will be observed that, of course, the sums which were ultimately distributed under the profit and loss account, although undoubtedly profits, were profits which would have an origin earlier than the year in which they were distributed. I think I am right in saying that the obsolescence claim arose under an agreement which was made between the Chamber of Shipping and the Government after the E.P.D. had come to an end?—That is correct, the date being November, 1922.

And then, after that, there were repayments in regard to obsolescence, and they become, no doubt, profits, and in the nature of things they are profits which arose under that agreement?—That is correct.

BY THE COURT—What deferred repairs? Was there any agreement

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with the Government in that matter?—No, but the matter was covered under the Finance No. 2 Act of 1915.

Mr. JUSTICE WRIGHT—"Obsolescence" is really a misnomer. It was due to the building of ships at the very high costs which were ruling at one time.

By Mr. PRATT—It has been pointed out that some "minor showers after the storm," as it were, went on until 1930?—Yes.

The fact that things were not finally cleared up was known to you in 1927?—Yes.

It was not thought sufficiently important to prevent you transferring practically the entire reserve?—There were specific cases left over.

By the COURT—You had really closed the whole thing in your books?—Yes.

A. F. LITTLE, examined by Mr. FULTON—I am secretary of H. & W. Nelson, Ltd., and the Nelson Steam Navigation Company, Ltd. I produce the minute-book of the Nelson Steam Navigation Company. It shows that at a meeting in May, 1913, Sir Owen Philipps (now Lord Kylsant) was unanimously appointed chairman of the company. The minute-book also shows that in the subsequent years the accounts of the company were considered by the board of directors. Lord Kylsant was present at each of the meetings, and signed as chairman. There was a meeting of the directors on 12th December, 1927. Apparently Lord Kylsant took the meeting, but the minute was signed by Mr. Lubbock. The minute of that meeting states that it was "resolved that a cash bonus of £200,000 be declared. Resolved that the offer of the R.M.S.P. to sell to the Navigation Company the whole of the issued and paid-up share capital of H. & W. Nelson, Ltd., at par, be accepted." The transfer was to take place on 28th September, 1927, less dividends and bonus declared, and be paid out of accrued profits. In addition, it was decided that 1,000,000 shares of £1 each should be allotted to the R.M.S.P.

I produce the minute-book of H. & W. Nelson, Ltd. It records that on 20th May, 1913, Sir Owen Philipps was elected as chairman of the company. There were meetings of the company in 1922, 1923, 1924, 1925, 1926, and 1927, mostly in the month of June, and there are records of the fact that the balance sheets and profit and loss accounts were before the board, and were approved. All those minutes were signed by Lord Kylsant as chairman. An extraordinary general meeting of the company was held in London on 30th December, 1926, when the chairman moved a resolution to the effect that it was expedient to capitalise £200,000 standing to the credit of the company's reserve fund, and forming part of the undivided profits. The directors were authorised to apply the amount in paying up in full 2000 shares of £100 each, which were to be allotted to the existing shareholders. Lord Kylsant was present at the meeting. On the same day there was a meeting of the board of directors, which Lord Kylsant did not attend.

## Evidence for Prosecution.

A. F. Little

Sir JOHN SIMON—This is a criminal case, and the Crown are ascertaining that neither of the two defendants was present at meetings, but minutes relating to those meetings are being read. It might be proper in a commercial case for such a procedure to be followed.

Mr. JUSTICE WRIGHT—It is not admissible. The actual language of the resolutions cannot be evidence against either of the two defendants if they were not present. The fact that a thing was done by the company can be established.

SIDNEY WALTER BLACK, examined by Mr. DEVLIN—I am an assistant secretary of the Royal Mail Steam Packet Company, and I keep the charters of the company. I produce a copy of the charters.

Cross-examined by Sir JOHN SIMON—I see from the charters that “the directors may, before recommending any dividend, set aside out of the company such sums as they may from time to time think proper as reserve, insurance, or suspense funds. All sums so set aside shall be applicable to meet any loss, the gradual liquidation of any debt or liability, or for repairing or renewing any property, or for equalising dividends, or for distribution by way of dividend or bonus which the directors might deem to be of advantage to the company, provided that only such portion of any reserve or other fund as shall in the opinion of the directors represent undivided profits properly available for dividend shall be distributed by way of dividend or bonus.” That is part of the constitution of the company?—It is.

Mr. JUSTICE WRIGHT—Is there anything in the regulations or the articles about the rights, or the want of rights, of the shareholders to ask for information?

Sir JOHN SIMON—I believe that in the case of this company there are no such provisions in its constitution.

ROBERT SMITH STEWART examined by Mr. PRITT—I am a chartered accountant and a member of the firm of Blease & Sons. My firm has acted as auditors for the two Nelson companies since they were incorporated, and has prepared the profit and loss accounts, and also attended to taxation matters. I personally have dealt with the duties of my firm to the Nelson companies. I produce the certified balance sheets for 1926 and 1927 of the Nelson Steam Navigation Company. These are both signed by Lord Kysant and Mr. Lubbock as directors. I also produce the certified balance sheets of H. & W. Nelson, Ltd., for the same two years signed by Lord Kysant and Mr. Lubbock as directors.

I have prepared a summary of the accounts of the two companies from 1921 to 1927.

One of the documents I have produced shows that in 1926 there was a transfer from deferred repairs reserve of £20,140, and from taxation reserve an amount of £29,860. There was a similar transfer from taxation reserve in 1927 of £131,035. In each of the years 1921 and 1922 both of the Nelson companies made a net profit. In June, 1926, the reserve of H. & W. Nelson, Ltd., stood at £200,000.



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Robert S. Stewart

Was a bonus declared in December of that year of 2000 shares of £100 each?—Yes.

As a result of that, was £200,000 put in the balance sheet as capital and taken from reserve?—Yes

And the capital of the company was increased from £50,000 to £250,000?—Yes.

Did you subsequently make some adjustment in the accounts in relation to that matter?—The taxation reserve account was transferred to reserve account.

Why did you do that?—It was on the instructions of Lord Kylsant.

Cross-examined by Sir JOHN SIMON—My firm had the responsibility of looking after the E.P.D. questions on behalf of the Royal Mail Group. Provisional figures were discussed year by year with the Inland Revenue, and I took part in the discussions.

So far as there was any agreement reached at first, was that agreement only provisional?—Yes, only provisional.

You say that in the year 1927 figures were arrived at which were more final, but the actual finality was reached in 1930?—The final settlement was 1930.

As between you and the Revenue, the discussion would be, would it not, as to figures for the group?—Yes.

And then the question of how the figure for the group was to be distributed among the different entities, the 100 per cents., and the R.M.S.P. would be a matter which the Revenue would have nothing to do with?—The Revenue would have nothing whatever to do with that.

The figure for 1917 was at one time assumed to be £586,198 for the whole group, but in 1927 the figure for 1917 was found to be £976,048. How much of that latter figure represented the R.M.S.P. Company's proportion?—£526,122.

Mr. JUSTICE WRIGHT—That is a new figure, so far as I can remember.

Sir JOHN SIMON—The reason is that up to this point your lordship has not had the figure as for a given year.

The WITNESS—From that figure of £526,122 there has to be deducted a nominal repayment to the R.M.S.P. amounting to £10,639, so that the net figure is £515,483.

*Cross-examination continued*—Is that an illustration of the way in which the provisional figures which were first discussed differed from the more final figures which were substituted in 1927?—Yes.

Mr. JUSTICE WRIGHT—Does the figure of £515,483 include the proportion for Meat Transports as well?

Sir JOHN SIMON—No. I have figures for other years, but in some years there was not so much contrast, or no contrast at all. For the year 1915, for example, the figures were practically the same as determined at the different dates.

The rate of duty was different in different years, and therefore it made a very great deal of difference how one allotted the figures as between one year and another. (*To witness*)—In these circumstances would it

## Evidence for Prosecution.

Robert S. Stewart

have been possible to have treated E.P.D. liability as determined and fixed in the year 1923?—Absolutely impossible.

I refer you to a letter written by Messrs. Blease & Sons on 28th December, 1923, in which they had stated that they had prepared an estimate of the liability for 1920. It goes on to state that, taking the figures so far as they were agreed with the Inspector of Taxes, together with the claim for deferred repairs, and making provision for adjustments, the figure would not exceed £130,508. What was in fact the figure arrived at for 1920 when the revision took place in 1927?—A deficiency of £294,327.

Whereas it was a liability in 1923, it was found in 1927 that it was not a liability, but on the contrary it was a cross-claim of £294,327. I think you were going to say that the figure differed more than that?—The liability amounted to £103,406; that is the figure by which the £294,327 should be increased.

By the COURT—Do you mean that the £294,327 should be something like £400,000?—I mean that for purposes of comparison the difference between the estimate and the final result is not as the difference between £130,508 and a deficiency of £294,327, but a difference between £130,508 and a deficiency of nearly £400,000.

*Cross-examination continued*—Was E.P.D. charged against the different firms and companies for different seven-year periods, according to the particular date in the year to which ordinarily they made up their accounts?—Yes; the period was seven years from the date of making up the last account prior to 4th August, 1914.

Re-examined by Mr. PRITT—Is it right that the total difference between what Sir John calls the original estimate and the actual result is just over 1 per cent.—£50,000 on £3,000,000?—Yes.

As between what was expected to result at the end of 1923 and what in fact did result in 1927 and 1930, was there any great difference?—No.

Did you in fact yourself form any estimate at the end of 1923 as to how things really stood?—Not an actual estimate of the liability.

A general idea?—Yes, of the position at that date.

Then at the end of 1923 you did hold a general idea of the position, subject to revision?—Yes.

And it actually came out in 1927 very much like your general idea of 1923?—Yes.

I suppose that all the time from the end of 1923 to the end of 1926 or 1925 the matter was gradually getting clearer?—Yes.

I suppose you were never consulted in any way by the R.M.S.P. as to how much of their E.P.D. reserve they should transfer to their profit and loss account?—No.

CHARLES SAMUEL LEWIS, examined by Mr. FULTON—I am chief accountant to the Royal Mail Steam Packet Company. In June, 1928, I was assistant accountant. On 8th June, 1928, when my chief, Mr. Cason, was on holiday, Lord Kysant sent for me, and said that he proposed to make an issue for the company, probably of 5 per cent.

# The Royal Mail Case.

Charles S. Lewis

debenture stock On that date the following was dictated to a clerk:—  
“ The audited accounts of the company show that during the past ten years the average profits (including profits of the insurance fund), after providing for depreciation and interest on debenture stocks, have been sufficient to pay the interest on the present issue more than times over.” Before that document was dictated, Lord Kysant informed me that he proposed to make the issue for four purposes—to meet overdrafts which the company had had at that time, to provide funds towards the cost of the new building in Leadenhall Street, for repaying one or two loans to associated companies, and for the general purposes of the company. He instructed me to fill in, after referring to the printed accounts of the company, the figure required. There is a pencilled alteration, the word “ profits ” having been altered to “ available balance.” I handed the document to Mr. Cason on 11th June, 1928, and at that time there was no pencilled writing on it.

Cross-examined by Sir PATRICK HASTINGS—Evidence has been given by Mr. Cason that in practice, after the accounts had been prepared by the accountancy department, they were submitted to the board, and, if the board approved them, they were sent back, and submitted to Mr. Morland with a view to his certifying them. When the accounts were returned by the board, were the words “ adjustment of taxation reserves ” written on them in pencil?—Not to my knowledge.

Were the words written in Mr. Morland’s handwriting?—I do not know.

Do not you remember his writing them when you and Mr. Cason were there?—I cannot actually remember him writing them, but I remember him discussing this alteration.

I want to get it clear that Mr. Morland said that in his view those words should go in, and that that was said in the presence of yourself and Mr. Cason?—Yes.

DAVID INGLIS CONRADI, examined by Mr. PRITT—I am secretary of the Royal Mail Steam Packet Company, and have been so for about a dozen years. I first heard of the proposal for a new debenture issue early in May, 1928. So far as I recollect I did not have any conversation with Lord Kysant about the matter at that particular time.

On 13th June, 1928, as we know from the minute-book, you were present at a meeting of the board of directors at which Lord Kysant was also present, and the minute shows there was a discussion on the new debenture issue, and authority was given to the chairman by the board to proceed in the matter?—Yes.

The matter was made a little more definite on 25th June of that year. An issue was authorised of £2,000,000 in debenture stock, and a prospectus was put before the board and approved subject to slight amendment?—That is so. I identify the prospectus, Exhibit No. 43.

That is signed by Lord Kysant “ Approved 25th June, 1928 ” ?—Yes.

I think before you saw that prospectus at the board meeting you

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David I. Conrad

had seen an early draft, or more than one earlier draft. Was the first of them Exhibit No. 44?—I may have seen an earlier one than this, I am not sure. I certainly saw this.

You are not sure whether you saw an earlier one than that?—Yes, I saw an earlier one.

The one you have in your hand is the one on which the word “profits” appears in pen, and “annual balance available” appears in writing, the word “profits” having been struck out. Would you look at Exhibit No. 45 and Exhibit No. 44? No. 45 is plainly later in date than No. 44 is it not? It has got the words “average annual balance available” in print?—Yes.

The document also has an addition to the effect that the company, in common with other shipping companies, had suffered from the general depression?—Yes. The words were written on a slip and pasted in.

Was Exhibit No. 43 the prospectus in very nearly its final form?—That is the one approved by the special court.

It has not got the important words beginning “Although in common with other shipping companies,” but it has got nearly everything else?—Yes.

Exhibit No. 44 is the earliest print of the prospectus that is now available so far as anybody can discover. It bears Lord Kysant’s initial, and it has a good many alterations in pen. It appears that when this document was actually printed the amount of the issue had not been decided upon, and £2,000,000 was written in. Do you agree that Exhibit No. 45 was later in date than the other, as it incorporates all the manuscript alterations in Exhibit No. 44?—Yes.

£2,000,000 is now printed in, and the words “average annual balance available” are also in print. In leaded type at one part of the document there appear the words “sufficient to pay interest on the present issue more than five times over”?—Yes.

Look at Exhibit No. 46. This bears the words: “No underwriting commission has been paid or will be paid.” Is that in Lord Kysant’s handwriting?—Yes.

Then Lord Kysant has also written on the side: “I approve of the two suggested alterations which I have marked ‘Kysant’”?—Yes.

Having received that, did you cause the prospectus to be printed and published and circulated?—Yes.

And it was, in fact, circulated to the public?—That is so.

Exhibit No. 47 is special committee book No. 1 of the company. Does that show that the allotment committee met on 4th and 5th July, 1928?—Yes.

Was Lord Kysant in the chair?—Yes.

And I think three other people were present?—Yes, three other directors.

Was it reported that there were applications to the total value of £3,274,000?—Yes. Applications came, in fact, from R.M.S.P. stockholders and associated companies’ shareholders to the extent of £1,300,000, and from the general public to the amount of a little less

# The Royal Mail Case.

David I. Conradi

than £2,000,000 The court of directors approved the allotment of approximately £1,106,905 to the R.M.S.P. stockholders and associated companies' shareholders, and £893,000 to the general public. The record produced shows a proposal that the managing director's remuneration for any year when a dividend of not less than 5 per cent. was paid on the ordinary shares should be a commission of  $\frac{1}{2}$  per cent. on the gross receipts

ARTHUR HENRY MILLBOURNE, examined by Mr. FULTON—I was private secretary to Lord Kylsant during the period 1912 to 1930. I remember the question of an issue of new debenture stock being considered in 1928. Lord Kylsant asked me to draft a prospectus for his consideration. I obtained an old draft and used it as a basis for the fresh one. The sentence beginning "although the company in common with other shipping companies," appeared in the handwriting of one of my assistants. It was written on my instructions. A slip bearing these words was handed to me by Lord Kylsant at his own house after an interview with Mr. Morland. He said that Mr. Morland had suggested that something of this sort should be added to the prospectus, and asked me whether I thought it might be added. I said I thought it might be added with advantage.

And as a consequence that slip was written out by your assistant and pasted into the draft?—Yes.

Evidence for the Prosecution closed.

## Submission by Sir Patrick Hastings for Mr. Morland.

Sir PATRICK HASTINGS—I understand in this case that Sir John Simon is going, at the appropriate moment, to make a submission to your lordship on the case. Inasmuch as I am only concerned for my client with one of the issues, it has been thought convenient that I should say first what I have to say on the matter.

Mr. JUSTICE WRIGHT—Who is the first on the record?

Sir PATRICK HASTINGS—Sir John is the first on the record.

Sir JOHN SIMON—I am prepared to take either course, but I agree with my friend. I should be very content to adopt what my friend says and add what I wish.

Mr. JUSTICE WRIGHT—Very well. I shall allow you to take any course you desire.

Sir PATRICK HASTINGS—May I just say a word first of all to make it plain, if I can, what the charge is that I am considering. I venture to think that there should be a close examination of the two charges. I am concerned, of course, mainly with the evidence to which I cross-examined, not unnaturally, and I want your lordship to consider the

## Submission by Sir Patrick Hastings.

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case which really is, in my view, equally applicable to both the defendants from the point of view which I am going to put before your lordship. We have now had from the Attorney-General a very clear exposition, and I think we now know what the points are, and I am just going to refer to a sentence or two in his opening which I think put quite clearly what the point is, as I understand it, upon the first two counts. Really they are the same in substance; I do not see any difference between them.

MR. JUSTICE WRIGHT—There are different acts in different years, and therefore they have to be separate.

SIR PATRICK HASTINGS—Yes, but apart from that the principle seems to be the same in both.

MR. JUSTICE WRIGHT—The language is the same.

SIR PATRICK HASTINGS—The language is precisely the same of both, and I think that with the exception that in one year there is one additional element, the facts seem to be the same in both years; anyhow, for the purpose of convenience I am going to treat them as though they were one. The charge is that my client aided and abetted Lord Kylsant in making, circulating, or publishing an annual report of the court of directors which he knew to be false in a material particular, in that the annual report concealed from the shareholders the true position of the company with intent to deceive the said shareholders. I am going to submit that there is no case for Mr. Morland to answer upon either of the charges relating to the two years in question. The profit and loss account is the document really in question. The balance sheet incorporates a summary of the profit and loss account. I am only anxious to see that I appreciate correctly the case that is made against me. I understand it to be this, that the misleading portion of the document is those lines in the profit and loss account which say that the balance for the year, including dividends on shares in allied and other companies, adjustment of taxation reserves, less depreciation of fleet, for the year 1926, gives a figure of £439,000, and for the year 1927, a figure of £697,000. I understand that those are the words which are said to make this balance sheet misleading; and it is supplemented, no doubt, upon the question of the intention to deceive by the view which, of course, I appreciate at once was the view which the learned Attorney-General held when the case was opened, that Mr. Morland was not wanting to sign the balance sheet without the words: "Adjustment of taxation reserves." In his opening speech the Attorney-General said: "In my submission to you that phrase 'adjustment of taxation reserves' was a phrase quite deliberately prepared and selected and chosen as a phrase which would convey nothing whatever to the mind of the ordinary person, but at the same time would enable anybody to say, in case the need thereafter arose: 'Oh, but this is covered by the phrase "adjustment of taxation reserves."' It betrays, in my submission to you, an uneasy conscience about what was being done." That was set out with great clarity, and I understand that is really the gravamen of the charge in so far as there is an intention to deceive—that those words were

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deliberately prepared, selected, and chosen as a phrase which would convey nothing whatever to the mind of the ordinary person, but at the same time would enable anybody to say thereafter, if the need ever arose, "all this is covered by adjustment of taxation reserve."

Mr. JUSTICE WRIGHT—One must look at this quite squarely.

Sir PATRICK HASTINGS—Of course I am only too anxious to do so. It seems to me that the first thing to consider is whether this can be called a false document.

Mr. JUSTICE WRIGHT—You remember under the new Act of 1929 as applied to chartered companies, there is a minor offence in which reference to intent is omitted; but the first question is, is it a false document? And if it is *prima facie* a false document, I should have to consider very carefully whether the matter would not have to go to the jury. If there is any ground for saying it is a false document, they would have to say whether it is a false document in fact; and, secondly, whether there was intent. I take it that the Attorney-General's case is that it is a false document, not in the sense that you can put your finger on any specific matter, but that, if you read it, it might naturally convey to any one's mind a view of the position of the company which was different from what its position actually was.

Sir PATRICK HASTINGS—I was going to say exactly the same thing, the other way round. I was going to suggest that before one comes to consider whether there was an intention to deceive one had to see whether the document itself was false.

Mr. JUSTICE WRIGHT—Clearly, because if it is not a false document, it really does not matter; you cannot consider the intent, because you have not laid the basis. If it appears to be a false document *prima facie*, then the question of intent and the question of fact are clearly for the jury; so that on this somewhat artificial method of approaching the matter I want your help first of all on the point of whether I ought to say that it cannot be regarded as a false document.

Sir PATRICK HASTINGS—My next sentence was going to be that you cannot consider whether there was an intention to mislead unless one sees whether the document is false.

Mr. JUSTICE WRIGHT—I entirely agree with that.

Sir PATRICK HASTINGS—In a sense it may be said that whether a document is false may depend upon two things; first of all, whether it is strictly accurate in fact, but it may also depend upon whether the general inference to be drawn from it is not strictly accurate in fact. I think it does give a little complication in this case.

Mr. JUSTICE WRIGHT—There is one thing I want you to consider: this is a balance sheet and profit and loss account. What exactly is the function of a balance sheet and profit and loss account, and what would you naturally expect to find in it?

Sir PATRICK HASTINGS—Not only has that been the subject of careful thought by us for weeks past, but one of the things that have been outstanding in our minds is: Why is it that, when the prosecution have called certainly one of the most distinguished auditors in the country—

## Submission by Sir Patrick Hastings.

Sir Patrick Hastings

possibly more—not one question has been directed to them with a view to assisting the jury on the very matter which one would have thought was a matter which was of very great importance. So far the only evidence that has been given by any witness at all touching upon these matters has been given by a witness for the Crown merely in cross-examination, the evidence given in that way being precisely the evidence of the presidents of the two branches of the profession. Some questions were put to Lord Plender which, I submit, completely dispose of both the elements in this case, both the suggested falsity of the balance sheet and also a point which I think is involved in the same consideration in the sentence which the learned Attorney-General used, as to this phrase which is, I think, the vital phrase, being deliberately prepared and selected for the purpose apparently of deceit. May I first of all consider this under the two heads? Here is a document, a balance sheet, and profit and loss account. I defy any one to tell the Court that there is the slightest evidence that every item in this balance sheet is not absolutely accurate and truthful. I refer to the balance sheet; I then turn to the profit and loss account, and I say exactly the same with regard to every single item in the profit and loss account. There is not one single item in this to which any one could take exception as a statement of fact in figures. That is the reason why I am satisfied in my own mind that the Attorney-General thought it right and proper and necessary to call attention to what he, I venture to think, suggests makes this document—which otherwise is absolutely accurate and truthful in fact—misleading.

Mr. JUSTICE WRIGHT—The shareholders of the Royal Mail Steam Packet Company seem to be very content with meagre information. It may be that that is not the point.

Sir PATRICK HASTINGS—I venture to suggest it is not. If the question of adequacy in form, otherwise than accuracy in figures or accuracy in words, was required, and if the question here had been one of adequacy in form or information given in form, hundreds of balance sheets could be produced, but the Attorney-General, quite frankly at the opening, said other balance sheets did not help us.

Mr. JUSTICE WRIGHT—Of course he could not say anything else; but really, quite apart from any technical aspect of the matter, it does seem to be an extraordinary thing that this company should go on year by year, as we know it was going on, without the shareholders being told something in terms as to what was happening. But it may be that that is not a question for the Court at all.

Sir PATRICK HASTINGS—I am glad your lordship has put that matter at such an early stage, because I am so anxious to deal with it. Can it possibly be said that it is a question as to the truthfulness of a balance sheet, of a profit and loss account, if the figures are given properly and accurately? The evidence establishes beyond all question that the very words used in this balance sheet and profit and loss account were those which would meet with the approval of the most distinguished auditors and qualified people in the country. Now can it be said that that is not truthful, accurate, and proper?



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Mr. JUSTICE WRIGHT—An auditor might say that this was a matter between the shareholders and the court of directors; if the shareholders were satisfied to open their mouths and swallow what came, it might be that it did not concern the auditor. That is one of the things which will have to be considered

Sir PATRICK HASTINGS—Surely, with great respect, your lordship must remember that Mr. Morland is now standing in the dock on a criminal charge.

Mr. JUSTICE WRIGHT—I bear that in mind. That is why I say one has to be careful to appreciate exactly what is the function of a balance sheet and what is the function of the auditor.

Sir PATRICK HASTINGS—Lord Plender told us what was the position of an auditor, and what he, with all his experience, would consider was the result of the information conveyed by this profit and loss account. To my mind it is so important that I am going to ask your lordship to allow me to read a few passages from Lord Plender's evidence. In cross-examination Lord Plender has made it quite plain

Whatever we call them, it is the practice of many of the largest commercial enterprises in the country to have a system of either secret internal or inner reserves, call them what you will, is it not?—Yes.

It is quite usual for large commercial and industrial companies to set aside, out of an unusually prosperous year or series of years, sums to an inner or internal reserve?—Yes

Now I want to go to a specific case. It is quite usual and a proper thing, or rather it was, for companies to set aside large sums against their liability for excess profits duty?—Yes They know that a liability would mature some day, and as prudent people they would make such provisions on account as they thought were suitable to make to meet that liability when it matured.

In the ordinary case such reserves would be set aside out of the profits of the year, would they not?—Yes.

I just want you to take the case where they were not required; in such a case when it was discovered, if it was discovered, that they were not required, they would properly be brought back into the profits for subsequent years, would they not?—Quite a regular credit.

I think the Attorney-General told us yesterday that in his view, up to a point, those secret reserves, being brought back, in many cases would not be disclosed in a profit and loss account as having been brought from secret reserves?—Sometimes no reference is made, but, generally speaking, it will be found that an indication is made that some transfer has been made.

Do I understand you to mean by that, that if the secret or inner reserves are used for that purpose there comes, or probably might come, a time when an auditor would say that some indication should be given to the shareholders that these transfers are being made?—Yes. . . .

I do not want to go through other cases, because, as the Attorney-General has told us, it is always difficult to judge another case without knowing the full facts, but in your view does this fairly describe it? Supposing you have, let me say, a large surplus which has been reserved for excess profits duty. That would properly be included in the balance sheet, would it not, in that item to which the Attorney called reference, "Sundry Creditors"?—Yes.

Assume there was an occasion in some year to bring back a sum to the credit of profit and loss because you did not require your excess profit duty reserve, it might very well be that in the first year that it was done no reference would be made in the balance sheet to the fact that it was brought

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forward at all?—You mean no reference would be made in the profit and loss account?

I ask you to assume that I have many balance sheets here which I have examined. There are many cases in which one may take the first year—an occasion when there is no longer a requirement to keep a reserve for excess profits duty, that is introduced into the credit of the year's profit and loss and no mention is made on that occasion that reserves have been called upon at all?—There are such cases

Mr. JUSTICE WRIGHT—There are two stages; the first stage is the appearance in the balance sheet of the sum which has been put to reserve because it must appear in the balance sheet somewhere or the accounts would be wrong, and it must appear under some heading. It is only called an internal reserve because it is specifically described as a reserve, but it must appear under some heading, and I think it is with that matter in view that, when the question was asked, Lord Plender answered as he did, because he means there must be a reference in the balance sheet when it is put to reserve.

Sir PATRICK HASTINGS—The question I was addressing to Lord Plender was necessarily dependent on the case which was going to be made against me. I was not sure whether the Attorney-General was going to say it is a proper thing or a legitimate thing to take a secret reserve and put it into your balance sheet as a reserve that would be allocated to sundries, and, further, whether he was going to say it is legitimate in some cases and up to a point, and thereafter to bring it into the profit and loss account without disclosing it, or whether he was not. In either case I was prepared to deal with the matter through Lord Plender, but the Attorney-General made it quite plain in his opening that he adopted the former course, that it was unnecessary for me to cross-examine Lord Plender to establish (a) that it is legitimate to put sums to secret reserves, and (b) that it is legitimate up to a point to bring them into the profit and loss account without disclosing it, because the Attorney-General assumed that in the purpose of his opening. Therefore, the first part of my cross-examination, which I would have directed to Lord Plender in the other alternative, was not necessary. We started this case on the assumption that up to a point secret reserves in the balance sheet were legitimate, and transfers from secret reserves to profit and loss account without disclosure up to a point was legitimate, and the Attorney-General said in opening: "There comes a point where it must stop." That is the case, and therefore the questions I put to Lord Plender were really, if I had been strictly accurate, a waste of time. They were only introductory to bring Lord Plender's mind back to the point which followed after the Attorney-General's admission, namely, what was to happen then, and the only reason why I asked the questions was this: Lord Plender said there are such cases, and then your lordship said: "You mean that has been done?" and he said "Yes, it has been done." I thought there was some ambiguity about that, so I said: "I want you to tell me this; is it done by firms of the very highest repute?—Yes." I said I did not want to go into individual cases. Obviously one does not want to

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go into other accountants' businesses. "In your view no exception could be taken to that?—As a principle, no exception could be taken."

Mr. JUSTICE WRIGHT—It is a very properly guarded answer, as a principle, and I suppose nobody would dispute that as a principle.

Sir PATRICK HASTINGS—Then one starts with the assumption that up to a point secret reserves are legitimate, and, I was going to say, ordinary. A transfer of secret reserves without disclosure into the profit and loss account is ordinary and legitimate, but there comes a time which the learned Attorney-General said might be and must be very difficult to determine, when some indication has to be given; and the whole cross-examination was based on this. It is no use looking at a balance sheet and saying merely "It is not quite accurate in the sense that it does not disclose secret reserves," because Lord Plender and the Attorney-General have said it is frequently done. There is no mention of adjustment of taxation reserves or anything—simply a balance of the year and an amount brought in from secret reserves, and no mention of it at all, and the mere fact that that appears in one sense may be said to be untrue, if you scrutinise the word "balance"; but the evidence for the prosecution and the opening for the prosecution is that that is legitimate up to a point. It was therefore necessary that Lord Plender should be cross-examined as to what was the duty of the auditor when that point arrived.

Do you agree with me that if an auditor were engaged there would come a time when the auditor would say "Now if those reserves are to be used again, some indication must be given to the shareholders that the profit and loss account is augmented by transfers from the excess profits duty or other reserves"?—Yes.

Now, there, Lord Plender is quite clear that a time might come when some indication, to use his own words, has got to be given. Then I am vitally concerned to see whether the time has arrived, whether I gave one, and whether I gave the proper one, and whether it is one which a person looking at it could understand, and which conveyed the necessary inference intended to be conveyed. Then I said: "Are there some well-known phrases?" and your lordship said: "Well known to whom?" and I said: "To auditors."

Mr. JUSTICE WRIGHT—You said "To auditors," but I really meant was it well known to many members of the public, but you took the auditor's view and I did not trouble any further.

Sir PATRICK HASTINGS—Your lordship may remember I did ask Lord Plender about other people, and he said, and I rather agreed, "Do not ask me about other people; I can only answer for myself and my own profession."

I should like, if I may, just to complete this part of the case, because I should like now once more to bring to your lordship's mind the phrase which seemed to me to be so important on this part of the case, and I think, if I may say so, not unnaturally, having regard to what we now know happened. "Adjustment of taxation reserves," said the Attorney-General, "was a phrase quite deliberately prepared

## Submission by Sir Patrick Hastings.

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and selected and chosen as a phrase which would convey nothing whatever to the mind of the ordinary person, and was therefore dishonest."

Is it usual among accountants to employ such phrases as these: Excess profits duty adjustment, after adjustment of reserve for excess profits duty, after adjustment of reserve for excess profits duty, after adjustment of income tax not required, taxation adjustment, adjustment of taxation reserve? Are all those phrases phrases which are not uncommonly used by an auditor to indicate transfers from taxation reserve?—That is so

Those transfers according to the facts of any case might be either large or small?—Yes

Then I read a further passage from the learned Attorney-General's opening:

I do not doubt that a sum reserved is by no means infrequently brought into the profit and loss account either to do away with or diminish a loss or turn the loss into a profit.

Lord Plender said he was not in Court the whole time, but he accepted that.

That being so, if you saw such words as those which I have described in a profit and loss account, you would understand from them, would you not, that there had been a transfer from the special reserve for excess profits duty or otherwise which might be small or large?—Certainly

By the Court—Would you translate the word "adjustment"? What does it mean, exactly?—The definition I would give it is this, the difference between a sum or sums reserved or set aside to meet maturing obligations whose precise ascertainment is not known at the time such provisions are being made, and the amount of the actual liability when it is ascertained and settled.

That is the answer of Lord Plender. I then went on to deal with some other points for a moment about transfers. I asked him to take in his hand a copy of the balance sheet in respect to which Mr. Morland is charged with using, preparing, and selecting a phrase which would convey nothing whatever to the ordinary mind. I asked Lord Plender to look at the figures, and then I asked him this question:

"Adjustment of Taxation Reserves"—you have told us you would understand from that that it had also been made up by a transfer from the taxation reserve account?—Yes.

I ask your lordship to say what can be left in respect to which Mr. Morland should be allowed for one further moment to stand in the dock, except this possible consideration. Would not the only thing that could be said against it be this, that it is possible that Mr. Morland used the regular recognised phrase among accountants? Perhaps it might be said an accountant would understand it when he wrote or read it, but it is just possible to say it may be a question of fact whether that strange being who is unknown to any of us called "an ordinary person" would understand it. Surely that is not the test. Here is a balance sheet going out to millions of pounds' worth of people in the City—solicitors, auditors, bankers, rich men, poor men, down to the ordinary person who perhaps lives miles away in the country, and does not understand in the slightest degree anything about it. Every

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one of those persons would be expected, if he had the slightest doubt as to the position and the amount, and thought it proper to ask, to go to the general meeting and say: "What is the amount?" An auditor is entitled to assume that that is the common form, that is the recognised and well-known form, and if anybody wants to know any more it may well be that Lord Plender might have said: "My competitors are such that I think it is in the interests of my shareholders that if they ask me the question I would advise them to leave the matter as it stands." But Mr. Morland cannot assume all that. That is the recognised expression used by accountants. May I ask your lordship to bear this in mind. After Lord Plender has been called and said it, not one single question has been put by the Crown to any accountant to disagree in the slightest particular with the evidence of Lord Plender, or to suggest from first to last that there is anything in this document which, not "would," but "could" mislead any person of ordinary intelligence who might be expected to peruse these accounts. Sir William M'Lintock goes into the box and not one single question is put to him as to whether he disagrees with the view that that is a perfectly good indication of the material fact we are considering. Not at all. Messrs. Blease go into the box, and not a question. There has not been a single question suggested to a living soul to suggest that that is not a perfectly proper document to put forward—not one—and after the cross-examination of Lord Plender I submit he has stated that it is. I ask your lordship to say that on that evidence it cannot be right that Mr. Morland should for another moment be standing where he is, after the evidence which has been given by Lord Plender, in effect, saying that the document conveys to the world the very thing which an auditor, if he was careful, would say at the very moment when they ought to know.

The Court Adjourned.



**Sir Patrick Hastings, K.C.**

# Submission by Sir Patrick Hastings.

Fifth Day—Friday, 24th July, 1931.

SIR PATRICK HASTINGS—Since the Court adjourned last night, I have devoted some little attention to the questions which your lordship was good enough to put to me in the course of the submission that I was making. The first question that I have been considering is the question as to what is the province of a profit and loss account and of a balance sheet. It is either a term of art, which I do not for a moment suggest it is; if it were, of course it is a matter in that case for the prosecution to explain, and there has been no evidence of any kind with regard to that. I venture to think that one cannot get a better general definition of the purpose of the balance sheet than that which is contained in the auditor's certificate, which is practically in the statutory form, which has to be attached to a balance sheet.

The balance sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company.

MR. JUSTICE WRIGHT—There are certain requirements under the new Act of 1929.

SIR PATRICK HASTINGS—Yes, under sec 124 of the new Act the statement as to what it shall contain is this—

Every balance sheet of a company shall contain a summary of the authorised share capital and of the issued capital of the company, and its liabilities and its assets, together with such particulars as are necessary to disclose the general nature of the liabilities and the assets of the company and to distinguish between the amounts respectively of the fixed assets and of the floating assets, and shall state how the values of the fixed assets and of the floating assets have been arrived at

That is the new Act which came into operation after much consideration

MR. JUSTICE WRIGHT—It does not apply to chartered companies

SIR PATRICK HASTINGS—No. There is a little further guidance in a document which is before your lordship, a little red book which Lord Plender put in, in which he sets out quite clearly his view of a balance sheet.

Every balance sheet is a summation of facts and opinions which should represent what, in the judgment of the directors, is a fair statement of the financial position of the company, having regard to the object for which it was formed and the existing circumstances and future maintenance of its business. It should be drawn up in such a manner as to afford the shareholders an adequate means of ascertaining, by perusal and inquiry, the value of their interests without disclosing information likely to cause loss or injury to the business. It is the province of the auditor to apply his trained mind to a critical examination of the balance sheet with a view of seeing whether, in his opinion, it substantially fulfils these conditions. He is not required to certify to an exact state of affairs, but he must be satisfied, in the light of the evidence available to him, that the balance sheet is properly drawn up in accordance with customary usage.

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I venture to think there could not be a fairer or more accurate view of the purpose of a balance sheet and the principles underlying its preparation than that, with which I am sure every one would unhesitatingly agree. I am bound to call attention to the fact that not one single professional man has suggested that in any respect, after examination of the figures, this balance sheet or profit and loss account is (1) untrue, or (2) misleading, in any way whatsoever. My case is—and I am going to call evidence to prove it—that every statement in this balance sheet in fact and by proper inference is absolutely true. The present question is whether there is any evidence at this moment that this document is untrue.

Mr. JUSTICE WRIGHT—There is a difference between no evidence and no sufficient evidence. The jury have the right at any time, having heard the case for the prosecution, to say that they are not satisfied, and subject to the right of counsel for the Crown to address them before they come to a final decision—a right which I do not imagine is often exercised—they may stop the case. But it is a very difficult matter to ask the judge to stop the case. He must be satisfied as a matter of law that there is no evidence. I mention that because, when you talk about professional usage and matters of that sort, those are eminently questions for a jury in the City of London. The question of intent is always one for the jury; whether these documents are sufficient and proper according to professional usage is purely a matter for the jury; it is their function, and I must not usurp the function of the jury.

Sir PATRICK HASTINGS—Of course I would not invite your lordship to do so, but I am bound in the view that we take of this case to submit the point which is proper for your lordship's consideration alone, that there is no evidence at all that this document is false.

Mr. JUSTICE WRIGHT—To say that there is no evidence at all is to say something which is a proposition of law. It may well be that you have a document which in every detail is technically correct, and yet such a document may create a false impression. Then, if that is a possibility, is not a question for the jury, who have to answer two questions, and possibly more? First of all, was it such as to reasonably create a false impression; and, secondly, was it intended to create a false impression? Those are two quite separate questions, each vital; but the mere fact that you can analyse a document point by point and say that there is nothing inaccurate in it is not conclusive.

Sir PATRICK HASTINGS—May I say that if I had been merely going to address your lordship upon the suggestion that statement by statement the balance sheet and profit and loss account are true, of course that alone might not be sufficient to found a submission upon. But in my submission the case goes far further than that. I submit that on the documents as we now know them, and on the facts as we now know them, there is no possibility of this document being untrue.

Mr. JUSTICE WRIGHT—The Attorney-General has placed the documents before the jury for their consideration. He says they may involve the view that the company was trading profitably. I would hesitate



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very much indeed in a case of this sort to withdraw the matter from the proper tribunal—the jury are the judges here—unless I am able to say as a matter of law that there is nothing which they can consider

SIR PATRICK HASTINGS—May I say at once that I so entirely accept that proposition that I was going to direct myself simply and solely to the point that there is nothing here which your lordship should leave to the jury, by reason of what I suggest is the necessary legal effect of the document itself and the facts as we now know them. From every aspect, in so far as it affects my client, the only two suggestions made in this case on behalf of the Crown were based on the words “Adjustment of taxation reserves,” and the statement made by the Attorney-General who said that “obviously there comes a point at which the continued and deliberate and excessive utilisation of hidden reserves quite manifestly presents an untrue picture of the company, viewing the enterprise of the company as a continuous and continuing whole.” The whole of the learned Attorney-General’s argument was based on a false supposition—false in this respect, that I am sure, now that he has heard the evidence given, he must be taken to know that all this talk of secret reserves is quite fallacious. The only person who ever made use of the expression “old reserves” was Sir William M’Lintock, who never asked Mr Morland a single question regarding the matter. The suggested secret reserves are two; one is income tax reserve, and in those cases there was no reserve at all; they were moneys obtained in the year and paid in the year; and the other was excess profits duty, and was not a secret reserve at all. I refer to a passage in Sir William M’Lintock’s cross-examination.

Is it your evidence here to-day that so far as regards any transfer of excess profits duty account in 1926 or in 1927 the company at the time they made that transfer were consciously drawing upon as ascertained-to-be old free reserve?—Yes.

That is all wrong. There again I do not want to go further into that.

MR. JUSTICE WRIGHT—The position as to what is sometimes called “secret reserves” is perfectly clear; I imagine the jury understand it quite precisely.

SIR PATRICK HASTINGS—I think so too, but your lordship does appreciate the enormous difference that that makes to the whole of this case as it is presented. But the fundamental principle underlying it is that to say, as Sir William Jowitt said, that the company is inevitably drifting on the rocks is to present an absolutely untrue view of the company’s prospects. The position is now established beyond all question, that at the time when this profit and loss account was issued, quite apart from the figures we have been discussing in this case, the company had in its coffers, over and above everything that was required to pay the dividends in question, an absolute disclosed reserve of one and a half million pounds and a reserve in the insurance fund of £1,300,000, and they had reserves in the subsidiaries of £2,000,000; that is £4,750,000 reserves over and above and not allocated to any purpose—reserves which could be used quite irrespective of these

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matters which have been dealt with in this case; and the only reason—the only conceivable reason—why this company might be said to be drifting on the rocks had nothing to do with its financial position at all. The real position of the Royal Mail Company, and the sooner it is made clear the better, was this, that like every other shipping company, like the banks and bankers—if things do not get better, the shipping companies will and must be, and the bankers possibly will be, on the rocks. But is any one going to say in a criminal Court that it is misleading because the auditor does not say to the shareholders: “I warn you that unless business improves, this company, like every other company, must be ruined?” That is the allegation. It is an appalling and a dreadful proposition to bring forward in a criminal Court. I say, without fear of contradiction, that if Mr. Morland, having seen those balance sheets in 1926, was guilty of a criminal offence, there is not a single accountant in the City of London or in the world who is not in the same position. He could not, without ruining this company, have taken upon himself the obligation of saying that which the learned Attorney-General said was the true view of the company’s prospects. It cannot be suggested that a man in this position is to be tried in a criminal Court, because he does not do—what? What ought he to have said? He ought to have said: “This company has paid its dividends properly; it has got reserves of £4,750,000, but unless there is a turn, unless trade in the shipping world with France, Germany, and America improves, it is inevitable that this shipping company cannot indefinitely go on.” It would ruin it. It would ruin every company in the world, and yet that is what is being asked.

**Mr. Justice Wright**—Surely these are considerations which may well be left to the jury. I am not trying this case.

**Sir Patrick Hastings**—Is not the true fact here that there is no evidence at all that this could be misleading? Those are the facts, and I ask your lordship to say that there is really no evidence at all which could properly be left to the jury; I ask you to say that in the case of Mr. Morland there is no evidence, or else that in your lordship’s view this is a case which should not be left to the jury.

## Submission by Sir John Simon for Lord Kysant.

**Sir John Simon**—I desire to make a short submission for Lord Kysant. I will not go over the ground which is so familiar to your lordship as to the function of a judge and jury in these matters. But what I should like to do is to see if I can by any chance be of any assistance to your lordship on the particular section under which this prosecution is launched. The inquiry in this Court is not whether further disclosure would be useful, or helpful, or desirable, or any of those things.

**Mr. Justice Wright**—Or proper.

## Submission by Sir John Simon.

Sir John Simon

Sir JOHN SIMON—The question is whether a particular section of the Larceny Act of 1861 is a section which, now that we have come to the end of the case for the prosecution, can be said to give solid support for the continuance of this case. My submission is this, that that, which sec. 84 penalises, is not economy of information, but material falsity in the information which in fact is given.

Mr. JUSTICE WRIGHT—Economy of information is quite beside the question, unless what is stated, having regard to what is not stated, produces a false impression.

Sir JOHN SIMON—I invite your lordship to look at sec. 81. As I understand it, this sec. 84 is a section which is not aimed at penalising economy of information; it is a section which penalises that which is stated, if the man who states it knows that the thing so stated is false in a material particular. There are occasions, certainly in civil law, when what the law requires is disclosure, and I recollect in the course of the opening by my learned friend, the Attorney-General, he made reference to it by saying that what was wanted here was a little more disclosure. I can understand the sense in which those considerations do come in, but it is, in my submission, quite fundamental at this stage that you should consider whether sec. 84 is not limited in its operation to penalising the falsity of a statement, however exiguous, in contradistinction from either penalising economy of information or stimulating a greater amount of information. I do not know that we are concerned here with reasons, because here is the statute, but the reason is that here we are administering the criminal law, and if I may quote a very famous passage in a very famous judgment on this very section delivered in this very place, in the year 1869, by Chief Justice Cockburn, this is what Chief Justice Cockburn says—

Mr. JUSTICE WRIGHT—Is that the *Queen v. Gurney*?

Sir JOHN SIMON—Yes.

It is one thing that a man may make himself liable to an action, or may be liable to have a contract which he seeks to enforce held to be vicious and bad, because he had stated something which went beyond the exact line of truth, or has concealed some material facts which ought to have been known to the other contracting party; more than this is required to support this charge. A man may honestly misrepresent, that is to say, he may state as true something which he believes to be true but which turns out to be untrue. If he has given a warranty, or has entered into a civil contract upon the assumption of the fact in question, he may be liable in a civil action to be defeated, but that would not be sufficient for the present purpose. Here you must be satisfied that that which is alleged to have been misrepresented was known to the defendants to be false, and that acting upon that knowledge, and with the deliberate intention to deceive and defraud, they did that which is alleged to have constituted the criminal offence.

Mr. JUSTICE WRIGHT—Yes, no one could state it more accurately than that; but you will see the difficulty that one is in at this stage. A man may publish a statement which he thinks is a complete compliance with his duty, and at the same time it may be false. The fact that he is doing something which he thinks is complete and sufficient

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may be a complete answer to any case that he may have had any intent to deceive, and yet the statement may be false.

Sir JOHN SIMON—That is perfectly true I am therefore quite strictly limiting myself to the character of the statement.

Mr. JUSTICE WRIGHT—If it were a question merely of intent, questions of intent are always proper for the jury

Sir JOHN SIMON—I am not addressing your lordship upon that at all for the moment. I am addressing you with all the force I can on a matter which seems to me very important here, namely, that in this criminal charge, sec. 84, rightly read, is a section which does not prescribe the punishment of the criminal law in respect of what I called economy of information, but is specifically directed to that which is affirmatively stated, and which is false in any material particular. I do not think you will altogether exclude from consideration those words. May I make one other observation also on the section? Lord Kysant is here under three counts, Mr. Morland under two; but your lordship observes that all three counts are in the same words and come under the same part of the same section. In each of the three counts the test is the same. It is not a question of what I have ventured to call economy of information; it is not the absence of full informatory matter which is the point in issue. The question is, what is it that is affirmatively stated, and is there at this stage material which will justify keeping this defendant in jeopardy in a criminal Court, the only charge on any of the counts being a publication of a statement, that means an affirmative statement—

Mr. JUSTICE WRIGHT—It means a document.

Sir JOHN SIMON—Yes, I think so; a written statement. It means not a thing by word of mouth, but it means that you have to consider what is affirmatively stated—published or printed—and it is not a point on a criminal charge to say in 1931, and looking back on the economic position of 1926 and 1927, that there are many things which it would have been wise, prudent, and proper to have stated.

Mr. JUSTICE WRIGHT—It is not a question of prospects; they are irrelevant in a case of this sort, as I think was pointed out by Mr. Justice Cockburn in that case you have been referring to. The material particular which it was said was false must have reference to existing facts. I should gather that that is covered by the form in which such particulars as there are are given in the indictment.

Sir JOHN SIMON—There are no particulars in the indictment, but I see what you mean. May I carry the argument a little further? What I have submitted first is that what is penalised by sec. 84 is not the limited character, perhaps the unduly limited character, of the information which is given. It is a section which is solely addressed to the falsity, to the knowledge of the accused—of course with intent—of the thing which is stated. If that were not so, this case would have taken a very different course from the beginning. The new Companies Act, which does not of course come into this case at all, is framed as the result of Mr. Wilfrid Greene's Committee's recommendations. In that

## Submission by Sir John Simon.

Sir John Simon

Committee's report the whole question as to whether or not you could call upon companies by law to state more precisely their reserves and their secret profit was ventilated, and a vast body of evidence was given to show what very serious financial results would follow if that was prescribed by law. When one looks at the new Companies Act, the singular thing is that when Parliament came to deal with the matter they still abstained from requiring by law under penalty that there should be disclosure, which is, as I conceive, the ground of complaint here. In my humble submission it is the function of the judge at this stage in a criminal trial, first, to satisfy himself as to the true construction of the section under which the prosecution is brought, and, secondly, to ask himself at this stage of the case, taking the evidence for the prosecution as a whole, whether there is any material. My submission is that really, as the matter now stands, there is no adequate material. I think references have been made as to how the Attorney-General put it. I do not mind how he put it. The question is: what is the present situation on the sum total of the evidence given for the prosecution? Neither do I in the least in the world mind that Sir William M'Lintock, in answer to a question from me, speaking I am sure with sincerity, told me in his view, as far as these excess profits duty matters were concerned, they came from old reserves. I registered his answer for the purpose of making sure that when later in the case I demonstrated that they were untrue, your lordship should realise that even Sir William M'Lintock has misunderstood the nature of this case, and nobody is to be kept in a criminal dock because Sir William M'Lintock has done that. It is now, in my submission, so clear that your lordship would never allow the liberty of a British subject to be left in jeopardy. It is now clear that, in point of fact, the different matters which were brought into the credit side of the profit and loss accounts in 1926 and 1927 in fact did not come from the old free reserves, but in fact were profits which were available for distribution at that time and not before.

Mr. JUSTICE WRIGHT—That is going into the facts.

Sir JOHN SIMON—It has been responsible for a great deal of trouble in this case.

Mr. JUSTICE WRIGHT—It may be, but after all, as you say, it is now a question of what the evidence is and what the facts are.

Sir JOHN SIMON—If your lordship thought it right to leave this matter to the jury, then nothing that has passed up to the present is of any prejudice to anybody. I take the view, and I submit it most strongly, that the section is a section which is addressed not to the encouragement of disclosure, not to the production of information, but simply and solely to penalising as a crime that which is false in a material particular to the knowledge of the author.

Mr. JUSTICE WRIGHT—I wondered at one time whether the true construction of this section was that specific words had to be pointed to which were false, but on reflection it seemed to me that was too narrow a view to take, and as nobody suggested that view it confirmed the conclusion to which I had already come.

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Sir JOHN SIMON—I hope your lordship will understand that I do not concede that specific words have not to be pointed to.

Mr. JUSTICE WRIGHT—If occasion arises, it is a point which you can always make. I have considered the matter in my own mind and I have come to the conclusion that it was too narrow a view

Sir JOHN SIMON—I have made my submission and, of course, nothing could be a graver matter for those who are now being represented here, but I do not desire to say more. I realise what your lordship has pointed out to my friend Sir Patrick, that, if indeed you thought it would be better for the case to proceed, the jury from this time forward are undoubtedly entitled to say that they do not desire it to proceed further; but if your lordship yourself did not say so, then, of course, I should wish to address the jury and to call evidence.

Mr JUSTICE WRIGHT—I think the case must proceed

## Opening Speech by Sir John Simon for Lord Kysant.

Sir JOHN SIMON—If your lordship pleases, members of the jury—You will, I am sure, have thoroughly understood that the discussion which you have listened to between counsel representing the defendants here and the learned judge, and the learned judge's decision on the point, has arisen both because it is very desirable at this stage to have the issues clarified, and also because it is our duty to get the judge's ruling as to whether the matter should, in his view, stop finally at this stage. You heard my lord take the view that he would prefer to leave the bringing of this case to a conclusion to the action of your own body after you have heard enough to satisfy you that you ought not to convict these two defendants, and Lord Kysant in particular, for whom I appear, on this criminal charge. It is very easy to spend a little time in rhetorical emphasis, to point out how serious a matter it is, and how humiliating it must be, to men who have borne a very honourable name to have to sit in this place while this criminal charge is investigated, but, after all, they look to you as a body of fellow-citizens who have been called here by the fortune of the ballot to do what is right.

I am going to call Lord Kysant. It is right that you should hear from his own lips what he has to say as to this most injurious imputation that he has been acting with intent to deceive, but before I call him I think you will excuse me if I occupy your time a little in bringing together what are the salient facts and features of the case. When those facts which have been ascertained are placed as clearly before you as they can be placed, and when the outstanding features of the case are disentangled from this immense mass of detail and figures, my submission to you is, trying Lord Kysant here on this criminal charge, he is entitled to your acquittal in the absence of firm proof such as would satisfy a reasonable man in his own case of guilt. My

## Opening Speech for Lord Kyslant.

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submission to you is the ultimate conclusion in this case you will find not to be in doubt.

Now, let me use such powers as I have to make clear what, as it seems to me, are the salient facts of the case. You have got a great company that has existed now for nearly one hundred years, the Royal Mail Steam Packet Company—one of those companies which have got a charter from the Crown, and therefore not a thing of mushroom growth, which has developed and become one of the great commercial institutions of our land. I do not think that anybody will doubt that it owes, and that every shareholder in it owes, a great deal to Lord Kyslant. It would have been perfectly possible for this great company to have distributed in its years of greater prosperity dividends far bigger than were distributed. Just let us look at Exhibit No. 105 and see what it says. There you have a series of seventeen years, the same seventeen years that are mentioned in that prospectus, and you see in column 2 what in fact was the rate of dividend which in the course of the very prudent management of this company was in fact paid. You see in column 7—for the moment I will take it down to, say, 1921 and 1922—the figure of the dividend that might year by year have been paid. Assume for a moment that I prove this document and it stands all challenge and tests, as I hope it will, and I think it will, is it not a very striking thing that over a very large number of years we have in fact a company which might have paid 13 per cent., 17 per cent, 22 per cent, and so on? Until you come to those two years 1926 and 1927, which have been selected for a criminal charge, the fact of the matter is that this great company had this great degree of prosperity. Why was it that it did not distribute everything that it might have distributed in these years of prosperity? Manifestly, because you are dealing with a branch of trade which has great fluctuations.

Whether or not there is a scientific basis for the view which is held by some economists and students that there really is a cycle, something in the nature of a recurring period, is a matter which you and I have not got to decide in this case. It would be very difficult to be sure, but many practical people have thought so, many business people have thought so, and you will be quite satisfied, when you have heard Lord Kyslant, that he, who has had a lifelong experience of shipping, was very strongly of that view. Not only so, but experience goes to show, as a mere matter of record, that there has been such a cycle in the past. Therefore if you conduct your company on conservative lines, if you abstain from paying out the whole of the profits you have made when the wave is on the crest, then you will be able to maintain, or you may hope to be able to maintain, a general level of dividend when the wave is in the trough. I quite agree that the view was taken by many people in 1927, even by some politicians, that there was a cure over the horizon for unemployment, that if only you voted for such and such a party things would mend; but the trough of the wave lasted quite unexpectedly long, and that is the

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life we are living through to-day. If the cycle of good trade had returned, as many people in 1927 and 1928 thought it would, and things had gone on an even keel and risen again, then, instead of Lord Kylsant sitting in the criminal dock here, he would have been acclaimed as one of the steady, sober men of British business who, in prosperous times, pursued a conservative policy and, in evil days, took advantage of that conservative policy in order to maintain his dividend, and who had got his fleet and his company out of a period of difficulty. But what happened is that in 1930, three years after the events we are now invited to investigate, unhappily contrary to the confident predictions of politicians, if indeed you set great store by them, contrary to the anticipations of many people studying the course of trade, a catastrophe, a calamity, overcame a very large part of the trade of the country, which has affected probably every one of us in some department or other. It is true that in the year 1930 the situation of the Royal Mail Steam Packet Company was such that it had to apply, itself or its subsidiaries, for the further assistance of the Credits Committee which the Government financed, because it was very difficult for it to deal with the matter unless the Government continued their guarantee to the banks for some time longer. Thereupon, extremely properly, Lord Plender, who was Chairman of that Committee, said: "I would like an independent investigation." An investigation is made, not for the purpose of finding out whether the accounts of 1926 or the accounts for 1927 are the basis of a criminal charge at all, but for the purpose of finding out what in 1930 were the prospects of prosperous trade for this company during the next year or two, because they wanted the Government guarantee to be continued, and the Government guarantee very properly was not likely to be offered to people unless they were able to show a prospect in the time that was then coming which would justify the Treasury and the taxpayer in lending them money in the meantime.

Sir William M'Lintock, as you have heard, makes a great report, nothing to do with this prosecution at all. I am not wishing to criticise anybody unfairly, but I think I am bound to say it is most unfortunate that that distinguished man in the course of it should have taken the view that there had been a drawing upon old reserves in the sense in which that view was presented when this prosecution started. I am going to remind you of what I believe has been proved to the satisfaction of every one of you during the last three days, and I am going to contrast it with that view. There cannot be the slightest question that when this case was first started, at the Guildhall, and afterwards here, until the gentlemen whom you have heard cross-examined during the last two or three days had given their evidence, there was a very widespread idea that this company in the later years was living on its own "fat." It was doing no such thing, except in this sense, that it was pursuing the policy of equalising its dividends by saving much of its profits in good years in order that it might be able to maintain a rate of dividend in less profitable years. But



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those dividends which were paid in these later years were dividends every penny of which was profits. I defy any sort of successful contradiction on this point, and I appeal to any member of your body who is in the least acquainted with accounts.

Now, what about the equalisation of dividends? There are two observations to be made about it. The first is this. It certainly cannot be a matter of reproach to the Royal Mail Steam Packet Company that it endeavoured to equalise dividends. That cannot be said, for you will remember I called attention to the fact that in this very charter—it would not matter if it was not there, but it is there—there is actually a provision which says (on page 49 of the charter) that the directors, after meeting contingencies, depreciation, and so on, are empowered out of their profits to accumulate or keep money for the equalising of dividends. And I know of no way in which you can do that—does anybody?—except that in the years that are prosperous you should distribute less. Now, why? Not, I apprehend, in order that you may put the balance into a drawer and lock it up, but in order that that balance may be available and may justify the maintenance of dividend in later years. Therefore, the first observation to be made on equalising dividends is this, that it is the specific direction of the charter under which Lord Kysant was acting that this is one of the powers which he and his brother-directors had for the good of the company. The other observation to be made is this, it is so easy to say, especially easy, perhaps, for those of us who have not had occasion ourselves to direct a great complicated concern of this nature: “Well, it is all very well not to distribute all your profit, but ought you not to tell the shareholders how much profit you have made?” What do you think would happen? Shareholders have got their full allowance of human nature. Two things would happen. One is that if you go out of your way to advertise, “We have had a boom year, but I am only going to suggest that you should get 5 or 6 per cent., although I could give you 17 per cent. or 15 per cent.,” what do you think would happen? The first thing that would happen would be, of course, a great demand by those who at the moment are shareholders to take there and then a larger part of the profit. What is the second thing that would happen? Any gentleman acquainted with business knows quite well that instead of the shares of the company standing, as they ought to stand, as far as possible without violent fluctuation, on the day when this is known or suspected, you start at once all those ups and downs which ought not to be, if things go reasonably well, the characteristic of a great chartered company’s issue.

I say in your presence, with the greatest possible confidence, you will find nobody who really speaks with authority in business or accountancy who is not prepared to recognise that it is right, in cases like this, not only to endeavour to equalise your dividends, but it is right in the years of prosperity—not, of course, to tell falsehoods, that is nobody’s right—to exercise that degree of economy in statement which reports that times have been fairly good, but which does not go on

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to say "And to let you into a secret, we have been doing so well that you might go out on the Stock Exchange and sell all your shares at a vastly increased value, and demand a vastly increased distribution." Nobody is going to say that. But what is the other half of it? If that is admitted, what follows?

Nobody is prosecuting Lord Kysant because in a specially good year he only proposed 5 or 6 per cent. to the shareholders. Nobody says "How disgraceful, a peer of the realm making a false statement, known to be false in a material particular. What could be more material than to know how much dividend you may get, and, though he has not said it in words, he has used language which seems to suggest that that is as much as ought properly or prudently to be distributed, when in fact he could distribute twice as much or three times as much." Nobody prosecutes him for that, but the other half of it, which fits it like a glove—the other part of it, which is the exact corresponding reciprocal position is this. When you come to times when you sink below the average level, and get, in the course of the cycle of trade, into the trough of the wave, are you then to go about and announce at every shareholders' meeting. "I want you all to appreciate that I am now drawing upon the conservative reserve which I made without telling you some years ago, and that is the only way in which you can get your dividends?" What would happen then? What would happen then would be that everybody would imagine that the ship, which in fact is merely sinking and rising, as it makes its progress across the sea of time is going on its downward course—is about to founder. There was no reason to think so, and no reason to say so, as I shall show you, I think, with the greatest clearness in a very few minutes.

Therefore my first proposition to you is this. If you look at Exhibit No. 105, it shows what was never, I think, shown clearly before, that as a matter of fact this is not a case in which the company went on paying 5 per cent. or 4 per cent. without justification, but it is a case where it was able to do so because of the very policy of equalising dividends, and acting in a conservative and prudent manner, which is the avowed intention of such great corporations. Where, I would like to know, would be the banks of the City of London if every year they were to state publicly exactly what has been the degree of prosperity or the misfortune which has overtaken them in the twelve months? Do you suppose that great enterprises of that sort jog along with an automatic standard level of profit year after year? I am quite certain that nobody with any acquaintance of business imagines anything of the kind.

My second proposition is, I want you to realise how the particular case here was regarded by those responsible for the prosecution at the time when it began. Just see what was the case which Lord Kysant was supposed to have to meet when the summonses were issued and when he surrendered before the Lord Mayor of London. In this passage, which was deliberately framed to state the submission of the Crown,

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Mr Pritt says "The submission for the Crown is that the words 'Balance for the year, including dividends on shares in allied and other companies, adjustment of taxation reserves, less depreciation of fleet, &c.,' coupled with the phrase below, 'Transfer from reserve fund,' is a clear representation to the shareholders that the company had earned in that year on its trading £139,000." I make this claim before you before I call any witness at all. I claim that every one of the four allegations has not only not been proved in this Court, but that every single one of them has been disproved by the Crown witnesses, and I am going to give you chapter and verse for that view. The first allegation is this: "It is a clear indication," says the Crown, "that the company had earned in that year on its trading £139,000, subject to some modest matter of adjustment of some taxation reserves." The very first question I put to Sir William M'Lintock was this. "Do business people and accountants draw a perfectly clear distinction between a trading account and a profit and loss account?" and he said "Yes." A trading account is an account which shows what you have earned on the one hand and what it has cost you on the other, and it shows as the result of the year the result of the trading operations and whether it is a profit or a loss. I turned to the profit and loss account for 1926 and said: "Is that document anything of the sort at all," and the truth is it is an absolute delusion to suppose that by examining this profit and loss account any reasonable person could draw any deduction whatever one way or the other as to whether or not the trading operations in that year show a profit or a loss.

I am perfectly content that you should pronounce at such stage as you think fit your view of these matters, but I think it is only right that it should be realised now by every one that Lord Kyslant was first brought before a criminal Court, and the Crown said what they believed no doubt to be the truth, because no one had been cross-examined then. "First of all," said the Crown, "you by publishing those four lines are stating to your shareholders falsely that £439,212 is a trading profit which this company has made in this year, subject to some modest adjustments," and Sir William M'Lintock said: "It does not say anything of the kind." It is utterly false to suppose that this document, with those four impeached lines, it making any statement whatever on the subject of the balance of the trading operations of the company for the year. I do not want to introduce any matter outside the evidence here, and I do not do so, but cannot you imagine many cases in which all sorts of phrases of a kind which do not state anything precise about the trading may be used? Has nobody ever seen the phrase "net result"? That is the result of bringing in those things which are proper to be brought in, and proper to be brought in in the year in question for the purpose of building up the fund on the right-hand side of the profit and loss account out of which will be met in due order the charges and the interest and the dividend. The plain fact is that these four lines are now understood by everybody, on the evidence of Sir William M'Lintock himself, not

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to make the smallest representation of any sort as to the trading results of the company for the year, but, on the contrary, they indicate a trading result which may have been a profit or which may have been a loss. A profit and loss account is not a trading account at all. A trading account, which may or may not be separately recorded, is a record of what has been the earnings of the company in the year, and you set against it the expenses of earning that, and then you get from that a balance which is merely an item which in due course goes to the profit and loss account. If you look at that little document, Exhibit No. 93 or 94, you will see that, as a matter of fact, I have put into that the profit of trading before charging depreciation.

In 1926 this figure of £439,212, which is the one we are discussing, is a composite figure, it is the result of a lot of things coming in. Some of them have nothing in the world to do with the selling of ships. If you want to know what the profit on trading was apart from depreciation, it was £35,106, just as in the next year the profit on trading before charging depreciation was £118,750; but the point is that anybody who is under the impression that this case could be proved against Lord Kylsant, because he puts his name to a profit and loss account with those four lines in it about the £439,212, by saying "Aha, that means you were telling your shareholders that you made a profit of something like that in the trading year," is wrong. It is admitted it does not mean it, and no intelligent person could suppose it could mean it. The accountant for the Crown says: "It does not even mean it is something like that; it is equally consistent with the view that it is a loss on trading which has been turned into a profit by other items." The learned judge put it in a single sentence very conveniently, I think: "There is nothing at all to indicate whether the trading operations of the company for that year showed a profit or a loss." That is the first point. The second point is it was suggested that the statement in the phrase "Adjustment of Taxation Reserves" was in fact conveying to those who read it that the alteration produced by bringing in other figures was modest and small. There, of course, as you have already been reminded, or as you heard Sir Patrick Hastings remind the judge, that again is a complete misunderstanding. You will remember, I am sure, that Lord Plender said adjustment of taxation reserves or some similar phrase has not got any implication of that sort, and what it does indicate is that whereas at some earlier time there may have been doubt as to how much should be reserved, in the meantime something has happened which has made it more definite—clarified it, as that admirable witness, Mr. Matthews, put it the other day—one of the clearest pieces of evidence I should think that has been heard in this Court for many a long day. The position is clarified, and consequently there is now something, which may be big or may be small, which can be transferred to the profit and loss account. I am sure you now understand the way in which accounts are kept in this regard is this: if you decide you are not going to distribute your 17 per cent. or 15 per cent. dividend in the year, but are only going to distribute 6 per cent., then you carry what you do not distribute aside

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as a security to the public who are going to subscribe, who will know it is a reserve and is there. It may be put on the left-hand side of your balance sheet under some general designation, sometimes by unduly depreciating your property. I have heard people say—I do not know whether it is true—that the building of the Bank of England stands in the books of the Bank of England at £1. I dare say it does. That merely means that the great National Bank has written down the value of one of the most valuable properties in the City of London to nothing at all. That is a way of securing a secret reserve. However you do it, you keep it out of your profit and loss account. Why? Because the moment you bring it into your profit and loss account in any year, from that moment it is released for the purpose of meeting the charges which are put on the other side of the profit and loss account. From the moment you pass, in the year 1926, let us say, £175,000 from income tax credits, or £550,000 from excess profits duty credits, into there, you are passing it into a compartment where it will make part of the total out of which you pay interest on your debenture stock, discount, dividend, and so on. That is the method followed in business, and it would be a most unhappy thing if here in the City of London, in a case in this Court, criminal though it is, we did anything to upset what is an essential part of the prudent carrying on of large classes of every great business.

If you were to go and state in a public document exactly how much you had transferred, you would be bringing about all the same consequences on the share market and in the minds of your shareholders as you are seeking to avoid by keeping a steady dividend. While, of course, no one is entitled to tell lies, it is at the same time of the essence of business that you should use in this matter what I will boldly call an economy of statement. It is perfectly legitimate when you are engaged in making a balance for the year which is going to supplement, it may be, your meagre trade returns, to move sums which are profits into the profit and loss account for the express purpose of increasing the credit side, and it is legitimate to do it without saying how much you are moving. A shareholder would be perfectly entitled at a meeting of the company to ask that the figure be expanded, but the chairman, if he is a man of character and integrity, and a man with a great commercial reputation behind him, who has helped his shareholders year after year by his special knowledge and devotion, would probably say: "Gentlemen, of course you shall have such information as you really desire, but may I tell you that the directors are strongly of the opinion that it is really in the interests of the company that you should put that amount of confidence in us to make this adjustment without telling you at this stage how these internal reserves now stand." If you do not do that, you start a speculation on the Stock Exchange which will "take the roof off" in the future if companies are to be conducted on these conservative lines. That is the second point, and I submit that without my calling a single word of evidence, it is completely exploded.

Now I am going to take the third point. It was said it must be

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relevant to the year, and that statement is a representation that whatever has been brought in is relevant to the year. Now, "relevant to the year," of course, might possibly mean either of two things. It might mean that the profits have been earned in the year. That is a conceivable way in which you might use the words, and I rather think it is the way it has been used sometimes in the course of the prosecution. The other sense in which it might be used would be that it became free to be distributed in that year. If it was supposed to mean the first of those two things, that is already disposed of by the evidence of the accountants, Sir William M'Lintock and others, to which I have called your attention, because, of course, as a matter of fact, if when you say this must be "relevant to the year" you mean it must have been carried in the year, that is merely saying over again it must be but the proceeds of the trading of the year. But we have already agreed it is not stating the results of the trading of the year at all, and, therefore, it becomes a piece of quite meaningless absurdity. The other question is, is it, as a matter of fact, brought in because this is the year in which it can first naturally be regarded as available for distribution, or is it from some old source where it has been kept, as it were, ready to be drawn upon, free at any moment but waiting for a rainy day? I am bound to tell you that I am quite at a loss to understand the proposition. I do not understand how any business could go on if it was not legitimate to put aside profits which have been earned at an earlier time and to keep them for a later time. I make the proposition perfectly plainly, that it is perfectly legitimate to dispose of profits which you have made and which are free, whether those profits are made in the same year or a previous year. What you may not do is to distribute them before they are made.

It was demonstrated in this case, and demonstrated before Sir William M'Lintock left the box, that £175,000 was relevant to the year in this, the very strictest sense, that the sums which made it up never reached the company until after the year had begun. You recollect, no doubt, that they were made up of three sums, or, strictly speaking, they were made up of four sums, three added together and one subtracted. One was a sum which at midsummer in the year 1926, when the year was half over, the company was at liberty to credit its income account with because the company sent out its dividend warrants on the 31st May. So when this company in the summer of 1926 was engaged in distributing the dividends of that year it was in the ordinary way entitled to deduct a very considerable sum, and it was there and then credited in the book. That was £121,000. The second thing they got in that year was a payment made by the Crown back to the company under a section of the Income Tax Act which gave you a sort of consolation prize if you were not doing so well as you were doing when you were assessed to income tax, and in that way they got £120,000. The second one was, I think, £70,000. That makes £190,000. The third one was a small matter of £5000. Therefore altogether there was £195,000 on the income tax account which actually fell into these ledgers in the year, and if it was not relevant to

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the year 1926, what year was it relevant to at all? All that has to be observed is that something had to be paid out in the year, and it was due to this, that if for any reason you got back this complicated excess profits duty business, one of the mysteries of the law is that what the Government loses on the swings, to a lesser extent it gains on the roundabouts. It says "Here is your excess profits duty back, and I am sorry to say I look too much"; and then they say: "Here, give me some of that back; I want it for income tax." Sir William M'Intock did not know that when he wrote his report and talked about old reserves, and when I drew his attention to it, he admitted it. You will recollect when Mr. Matthews came into this box I questioned him regarding the figures or sums which became available in 1926 and 1927, and he said that when those amounts did become available they were promptly transferred to profit and loss account.

When Lord Kylsant was summoned and brought before the Court in the City, learned counsel, presenting the case for the Crown said that the balance of £439,000 odd was only brought about by wholesale transfers from hidden reserves, which had got nothing whatever to do with the year in question at all. So that what was said to Lord Kylsant was: "You have criminally brought into this account by wholesale transfers from years before hidden reserves which had got nothing whatever to do with that year at all but which were existing there all the time," although when one begins to make the inquiry, where did these amounts come from? it appears they first reached this ledger in the very year they went out, and to a large extent they were paid in cash by a warrant from the Treasury to the R.M.S.P., and exactly the same thing in true about income tax reserve. That is not the whole case, I agree, but I claim to have established to you absolutely conclusively the evidence in this respect in all one way. Be it so, I take my stand with the greatest confidence that there is not a syllable of truth in the suggestion made when this case was started as regards the income tax matter, that they were sums which were not relevant to the year they were paid out. I do not think that the learned Attorney-General is going to reply by telling me here that he has got quite a different case than the case the Crown had when the matter came before the Lord Mayor.

I pass to the excess profits duty matter. In this wicked world in which we live, let us be at least grateful that Parliament has passed a law which says there is not to be any more of it, and although there will be no more of it the controversy which arose in the years after it was imposed was one of the most complicated, and I am bound to say most lucrative, controversies to accountants or lawyers. I am now going to summarise before you quite briefly, and as clearly as I can, the part of the case—a most important part of the case—which depends on excess profits duty. The point is a point of enormous importance, because very large sums were involved, of enormous importance because of the way in which it was at one time regarded and indeed prevented, and of enormous importance because, if the view that I have tried to

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bring out, and which has been confirmed by the witnesses, is understood and applied by you, that will at a blow explain away an enormous amount of misunderstanding which at one time seems to have prevailed on this matter. Excess profits duty is a duty that was put on, as you know, early in the war in order that businesses that were making more than a certain standard of pre-war profit should contribute, and contribute very handsomely, to the expenses of the country. Indeed, the duty had risen at one time to such a height that once you made in any year a profit which was bigger than your standard or datum, 80 per cent., or four-fifths of it, was taken for the general revenues of the country by taxation and you were only left with the other fifth; and it extended over a period of seven years. It came to an end in the year 1921. Of course, when it came to an end, as you realise, there was an enormous amount of discussion and negotiation and controversy between great businesses and the Revenue authorities in order to determine what the right charge was, and that went on for years. As you have heard quite clearly from Mr. Matthews and Mr. Stewart, in this case the thing was not finally decided certainly till 1927. It was a very difficult thing to do, and not at all a thing that could be shot at in the dark, because, of course, an immense amount depended upon the proper way in which you attributed particular figures to particular years. If it was in one year, the charge would be 40 per cent.; if it was in another year, the charge would be 80 per cent., and so on. I believe you must be now quite satisfied that in truth and in fact those figures of £550,000 in 1926 and £200,000 odd in 1927 which were taken into the profit and loss accounts, were taken in in their proper years. They were profits, of course; they had been frozen profits until they were melted and put into the profit and loss account.

You will remember I asked Mr. Matthews with regard to the figure of £232,788 in 1927: "Q. Is there any doubt that that item is an item which was properly transferred in that year?—A. No doubt at all; we could not have transferred it before. Q. You would not take the view, and I am sure have never expressed it, that this £232,788 was lying somewhere as an old reserve long ago, and that then in the year 1927 suddenly it occurred to you, 'Well, let us turn that into profit and loss account?'—A. No. Q. It was directly connected, was it not, with the events which occurred in the calendar year 1927?—A. Yes."

Now, could anything be plainer than that? I ask you in that connection to bear in mind what I quoted as being the submission of the Crown when these criminal proceedings were started, that those figures were brought about by wholesale transfers from hidden reserves which had got nothing whatever to do with the year at all, but which in fact had come from a couple of years before. Mr. Matthews says that the gentleman who gave that information at the time had not quite followed the situation, and it manifestly was so, and that is the end of that. In the previous year it was a round figure of £550,000, and that £550,000 is to be explained in exactly the same way.

You do not want to look at the thing years afterwards, and then, with all the added knowledge of what has happened since, try to



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imagine what might have been done, you want to look at it as it was looked at in 1926. There is a document which I introduced into the case called the balance proof, excess profits duty account, which gives you all the figures which explain the £550,000. If you look at the balance proof it appears that at the last day of 1925 in this excess profits duty ledger there was £390,277. Now, the first question is, was that £390,277 free before that date or was it, down to the beginning of 1926, a thing which is what I call "frozen," because it was not free. The answer is, you have only to look at the balance proof and you can see that according to the view of the company at the time there was a bigger prospective liability than they had provided for, and therefore they started the year 1926 by holding on to that £390,000. Then what happened in the calendar year 1926? You possibly may remember a phrase I used. I said that in a burst of generosity in the summer of 1926 the Revenue paid £330,000 to the company; and so they did, in the month of July. Of course, what I meant was at that time in that calendar year it was found by the Revenue that they had got too much, and they paid back £330,000, and that, therefore, was added to the £390,000. Now what was the company to do with that? The first point was this, that the £330,000 they got back from the Government did not all belong to the Royal Mail Steam Packet Company; £60,000 of it had to go to subsidiaries. That leaves them with £270,000 which the Government had given them, and £390,000 of their own. If you add those two figures together you will appreciate that they were now in a position to consider whether it was not possible in the year 1926, and because of what had happened in that year, to transfer a very substantial sum to profit and loss account, and they did transfer £550,000. They transferred £550,000 with all the more confidence, because, as a matter of fact, that is the year in which the obsolescence claim and the deferred repairs claims were, as between themselves and the Government, settled. Having transferred the £550,000, they were left with a balance of £110,000. The reason why they were justified in reducing the balance, which at the beginning of the year was nearly £400,000 to a balance of only £100,000 was, as Mr. Matthews put it, the situation was becoming clarified, by which he meant, of course, that the Government had at last agreed what was to be returned under the head of obsolescence allowance and under the head of deferred repairs allowance. It was true that there was still outstanding the actual settlement of what was to be done with regard to the excess profits duty, but it was not likely to be a very serious matter, and therefore he said: "We were justified in reducing our balance from £390,000 to £100,000." Could anything be clearer? The Act of Parliament itself which dealt with these adjustments of excess profits said that when money was repaid by the Government to the taxpayer on the excess profits duty account what was received should be treated, for income tax purposes, as income of the year in which it was repaid. So, if ever there was a thing which has been plainly proved by the Crown witnesses in the course of a case it is this, that, just as in the case of income tax, so in the case of excess profits duty, it is

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completely and absolutely wrong to suppose, as was supposed, and as was stated, that we are here in the presence of what was called a transfer of old reserves which had been free years and years before; and that is an error that I am very glad, with the help of the Crown witnesses, it has been possible to remove.

Now comes a very serious fact. It is no part of my business to utter a single word of rebuke or reproach against anybody, and I do not do so, but we must note that Sir William M'Lintock did not know those facts. He is one of the greatest figures in the world of accountancy, and has immense responsibilities on his shoulders. He was brought into this inquiry, not in connection with this criminal prosecution at all, but for the purpose of reporting to the Government as to the prospects of the future trading operations of the Royal Mail Company and its group in the year 1930, and I think it would be a very wrong thing to utter any word, even under the stress of defending an accused person in a criminal Court, which would seem to criticise him at all. When I cross-examined Sir William M'Lintock, I did call his attention to the income tax figures which we went through this morning, and Sir William said: "Yes, I see those figures, and I see it is so; those were sums which did arise in the year 1926, and which did arise in the year 1927." I put it to Sir William M'Lintock: "Is it your evidence here to-day that, so far as regards any transfer from excess profits duty account in 1926 or 1927, the company at the time they made that transfer were consciously drawing upon ascertained-to-be-old, free reserves; yes or no?" You may perhaps remember that he hesitated for a moment, because I was asking him a very detailed question; then he said "Yes." I said: "Then that is your evidence now?" and he said "Yes." Now, as I say, there is no question about making reproaches to a very great accountant at the head of his profession, but the fact of the matter is that Sir William, who is the head and front of the case, is demonstrated to be dead wrong by the evidence called in this case. Whether Sir William at that time was conscious or not that his information on this head was open to challenge, I do not presume to inquire, but I do know this, that when I asked him where he had got his information from he gave an answer which I also have had occasion in the course of the case this week to test. I asked him a number of questions, one of which was whether it would be all wrong to imagine that in 1923 the figures were finally settled, and in reply he stated that he had obtained his information from a letter written by Blease & Sons (the chartered accountants, of Liverpool), dated 28th December, 1923. Well, you know when a witness tells you that he took it from a document it is not a bad plan to ask to see the document. And what do you think it says? It does not say that all these figures were settled. It is a letter by Blease & Sons, Mr. Stewart's firm, to Mr. Cason, and it says: "Excess profits duty. We have prepared an estimate of the liability"—what liability?—for these seven years? Not at all—"for the year 1920. Taking the figures so far as they are agreed with the 'inspector of taxes' together with the claim for deferred repairs, and making ample provision for further adjustments,

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we consider that the liability will not exceed £130,000." But it does not stop there. For, as a matter of fact, even in his examination-in-chief, Sir William M'Lintock had used a most curious expression. He answered in a way which again is most unusual in a criminal Court. He was asked this question by Mr. Pritt: "Was a substantial amount of those reserves free from any period to the end of 1926?" and his answer was this: "Yes, it was known that there was a very large sum free about the end of 1923." I ventured to interpose, because "It was known" is a form of answer which I am not accustomed to, so I said: "I have not quite followed that answer." Then Mr. Justice Wright said: "It was known at 1923 that there was a very large sum which would certainly be free." Then my lord, not unnaturally, at that moment observed, "Of course, the excess profit duty had been practically ascertained." My lord was not meaning that he was satisfied of that, but that is what he understood at the time. Then Mr. Pritt, for the Crown, asked Sir William M'Lintock: "From what is your information obtained as to it being there," and the answer is: "My information was obtained from the assistant accountant of the Royal Mail, who dealt with taxation matters, and I was also shown a letter." I thought to myself: "Well, patience is a great virtue, even in the presence of one of the great heads of the profession, and in another day we shall see these people and, unless those who have been instructing me have completely misunderstood the accounts, we shall find that Sir William is utterly and entirely wrong." So, having been informed of this, I waited, and when they came I put to them, one after the other, the true facts, and as a matter of fact things were not settled till 1926 and 1927, but there were enormous differences, and Mr. Matthews told you that year by year, as soon as they could, they moved from excess profit duty into profit and loss as prudently as they could, as and when they received them. And lastly I put to them this question: "You surely never told anybody it was all agreed in 1923?" and the answer was "No." Then you will remember Mr. Stewart, the last witness. I put the question to him as to whether or not 1927 was the year. I asked: "That being so, I want to ask you this question. In those circumstances would it have been possible to treat the excess profit duty liability as determined and fixed in the year 1923?" and he replied, "Absolutely impossible," and gathered together a great bunch of papers in his two hands and he said: "Those sheets represent the summarised charges." Therefore, the whole thing is a complete mare's nest so far as excess profits duty is concerned, and the truth is this: There would have been no harm in it even if it had been true that in 1926 and 1927 the company had distributed its profits which had been reserved for bad times. To a limited degree it would appear to me to be a praiseworthy course rather than the opposite, but in truth and in fact neither the excess profits duty transfer, nor the income tax transfer, nor the corporation profits tax transfer, nor any other blessed item in those two little tables, Exhibits Nos. 93 and 94, were old; in fact, to say they are antiquated would be offering them too much insult. They are not even middle aged; they are, as a matter of fact,

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things which were available just at that time and were used as they came in.

Then the Crown, re-examining Mr. Matthews, who had charge of this part of the business, put this question to him, and I think the answer is very instructive, especially on the issue of intent. After all, if this is a crime we are investigating, the intention of the criminal is not unimportant. You will remember how my learned friend of the earlier stages put it to you this was a deliberate, cold-blooded, and ingenious scheme, by which illegitimate figures were put into the accounts of the year, drawn from long ago. When Mr. Matthews was being re-examined by Mr. Pritt, he was asked this question. Suppose the fact was that Lord Kylsant marched into the office and said, "Mr. Matthews, you must transfer so much; I am the authority to decide," that would have been one thing, but this is the question. My friend asked, "Who decides the precise figure to be transferred, as to how much is to be taken out of the excess profits duty?" and his reply was: "I suggest how much." Then my friend says: "To, I expect, Mr. Cason?"—A. Yes. Q. And you receive from Mr. Cason with or without delay a decision in the matter?—A. Yes." My friend was quite fair, as all prosecuting counsel desire to be, and he says, "Very often I suppose your suggestion would be adopted," and the witness says: "More or less."

Now I come to the last of the four heads of impeachment in this considered statement of the contentions of the Crown, so far as the original hearing was concerned, which is the most amazing of all. If once again you will be good enough to open this profit and loss account for the year 1926, and if once again you will just look at those four lines: "Balance for the year, including dividends," &c., you will see that in those four lines there is the word "Reserves"—"adjustment of taxation reserves." It is manifest, therefore, whatever else is not stated, that in that total of £439,000 odd there is included something from reserves. On that same page, three lines down, you will find that, in addition to that reference, there is also a reference to "transferred from reserve fund, £150,000." I should have thought that the very slightest examination of that document would have shown you that there are manifestly two transfers here connected with the subject of reserves. Yet, when this case was presented on behalf of the Crown, the fourth allegation made for the Crown was that the four lines: "Balance for the year" and what followed were a representation that the transfers from any reserve funds only amounted to £150,000. If anybody can seriously say that to-day, they can say anything. It is perfectly plain that there is a published reserve fund, but it is perfectly clear that this company was also a company which had, as so many companies have, internal, secret—I am not afraid of the word—locked up, additional reserves, most prudently put away. It is manifest to every one who looks at the document with intelligence that it would not be right to say that it is a representation that nothing has been taken from any reserves except from the published reserves. I am going to ask you, therefore, with the greatest confidence, to say that

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you are satisfied that there is no material here whatever at this moment which could possibly justify a conclusion at your hands that there has been the perpetration of a deliberately false affirmative statement or representation of any kind whatever. The only reason I say affirmative is because this section is not a section which says that everybody ought to disclose so much and so much, and in point of fact, even since these events occurred, Parliament, in passing the new Companies Act, which contains in some respects provisions calling for more information, abstains even to-day from saying that you have to disclose secret or internal reserves, or anything of the kind, and for a very good reason, because those of you who are acquainted with business will perfectly understand it would be a very bad day for British commerce and finance and industry if you did not put a proper degree of confidence in those who are continuously managing great businesses to abstain from distributing to the full the great profits which are made when things are prosperous in order that they may assist and alleviate those for whom they are responsible at a time when things are depressed. For the rest, it is so easy in 1931 to look back and say. "Oh, if I had been the chairman of the Royal Mail Steam Packet Company, I should have said more in 1927." How many politicians there are who tell you if only they had been Prime Minister in 1927 we should be in a different world to-day! You have to put yourselves back to 1926. That was the time when in shipping as well as in other things it was reasonable for people to think that the tide had begun to turn. Who is going to say of Lord Kyslant that he had no right to believe, that things were beginning to mend, and if, indeed, that which was a perfectly reasonable view to take then (whatever the wisacres may say in 1930 and 1931) had proved to be true, it is not in the dock that you would have found Lord Kyslant. There would have been an enthusiastic shareholders' meeting to congratulate him on the firmness with which he had maintained a conservative policy throughout the whole of a difficult time.

I want to say a word or two about the prospectus. I find it is quite impossible to take the view that the case on the prospectus, which is in effect Lord Kyslant alone, is a case which puts a new and a more difficult burden upon the defence, and I will show you why. We have heard very little about the prospectus, and I will not delay you longer than I need, but I wish to deal with it quite clearly before I call anybody. I am going to read the two paragraphs at the bottom of the second page. Those are the two which I think really matter. The first paragraph reads:

Although this company, in common with other shipping companies, has suffered from the depression in the shipping industry, the audited accounts of the company show that during the past ten years the average annual balance available (including profits of the insurance fund), after providing for depreciation and interest on existing debenture stocks, has been sufficient to pay the interest on the present issue more than five times over.

May I stop to remind you what was required to pay the interest on the present figure was £100,000; so that when it is said that it was

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sufficient to pay £100,000 more than five times over, that is the same thing as saying that the average annual balance available, including profits and after providing for depreciation and interest, has been £500,000 and more. Now, the first thing I am going to ask you to consider is: Was that true? Then comes the second paragraph:

After providing for all taxation, depreciation of the fleet, &c, adding to the reserves and payment of dividends on the preference stocks, the dividends on the ordinary stock during the last seven years have been as follows,

and they are set out. It is interesting and significant to note that if it had not been for the policy of equalising dividends as far as possible the figures for the first three years, for example, would have been far bigger, and I am not disputing the fact that it is the circumstance that they were kept at that level which enabled the figures lower down without greater difficulty to be kept where they were. It seems to me, subject always to what his lordship may ultimately say to you, that as far as there is any issue yet to be determined, I personally think it is all proved by the witnesses for the prosecution up to the present to be quite true. The issue consists of these two things. First of all, was it true in the fair sense, as between man and man, that during the past ten years the average annual balance available, including profits of the insurance fund, after providing for depreciation and interest, has been £500,000 and over? It is demonstrated already in the evidence given that it is true. I am sure you will bear it in mind. Secondly, it is true, that as between 1911 and 1927, after providing for all taxation and depreciation of the fleet, and adding to the reserves and paying these prior charges, it has been possible to make these dividend payments? Of course, when I say those are the two questions, there is also after that the question—well, if indeed anybody could say either of these things was false to the knowledge of the person who put it forward—was it said for the purpose of deceit? But let us begin with the question. Is it true or false? I take first the question of the annual balance. The whole point of this prospectus is that it shows deliberately to the person who reads it: "I am not giving you year by year a series of fluctuating figures; what I am telling you is, if you look through the ten years, these are years in which it is true to say throughout, after I have taken the depreciation, after I have taken the interest, and so on, there has on the average been enough to meet the interest on what we now ask to borrow, and five times more, and that is true." Really, members of the jury, do not you think the business of public life, or financial life, is becoming too complicated for human nature if you are not entitled to state: "This is the average, and I have taken it over a period, and I have endeavoured to keep my dividends steady." Nobody, in fact, supposes that a shipping company makes exactly the same profit every year; it depends on freight, on competition, and on finances; it depends on a hundred things. If a man is going to be impeached for carrying on the business of a great shipping company, trying always to produce for his shareholders a steady dividend, there is nothing, in my submission, which cannot be

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connected with this charge. I hope you noticed I put some questions to Sir William M'Lintock on the subject of depreciation, and I must say I should have been glad if he had seen fit to point out at a very early stage that, in fact, this company was being conducted on conservative lines, that it was year after year charging a rate of depreciation which experience shows to be excessive, which the Revenue knows to be excessive, and which Sir William M'Lintock, serving on a Royal Commission, had had before him evidence that it was excessive—apart from that, in the years of prosperity this company have taken one and a half millions and put it aside. If one cares for anything more than these general observations, they may observe this: These accounts here and there show the sale of a ship, and nobody has drawn my attention to a case where a ship was sold at less than its value. That shows the depreciation was overdone; they were continuing the plan, scheme, and practice of saying: "Let us distribute all this; let us write down these great ships of ours, so we know we have got on our balance sheet a figure which it is perfectly legitimate hereafter to realise." Sir William M'Lintock admitted in cross-examination that he had taken the usual 5 per cent. I remember I asked him the question: "Is that the usual figure?" and my lord pointed out to me I should ask him: "Is there a usual figure?" and I varied my question, and he said the only usual figure he knew was the Inland Revenue figure of 4 per cent. When you look at this prospectus you observe, when it speaks of "after providing for depreciation," it means this big depreciation, and I submit to you there is absolutely not a shadow of ground for suggesting that that paragraph in this prospectus has any taint of criminality from beginning to end. Observe one thing more. There appears to have been introduced at the beginning of it a warning: "Although this company in common with other shipping companies has suffered from the depression in the shipping industry." Have we had in evidence in this case that the other shipping industries in this country are booming? None at all. Consequently, what you find in this prospectus is this, that they are saying to the intending investor: "Now, do not imagine that this company is to-day not suffering from depression." What does that mean? It means: "Do not imagine that our trading profits at present are what they would be in time of boom." They say: "I am going to set out the figures which wear an air of integrity, and I am going to tell you we have been suffering from a depression, and the reason why that is not shown is what? The one and only reason that everybody does know is that Lord Kysant and his co-directors in the times when they were enjoying prosperity did not distribute all that might have been distributed and therefore could maintain a dividend in times of depression."

The only remaining question I can see on the prospectus is this, and really, gentlemen, with the great responsibility of all these three charges, I do not regard this third charge as one which is going to give you trouble. The last paragraph of it contains the statement: "After providing for all taxation, depreciation of the fleet, and adding to reserves." Now, when this case was opened, it almost appeared

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that the prosecution thought there had not been an addition to the reserves. It is extraordinary how confused some people can get.

The ATTORNEY-GENERAL—I did not say that; I said the contrary.

Sir JOHN SIMON—Mr. Attorney is kind enough to relieve me about that. Allow me to repeat to you, in his hearing, what he said. The fact of it is that the reserves were increased. There are two kinds of reserves; there is the reserve that is published and there is this internal reserve. I should think that every one of you will think that when there is a reference on page 2 of this book to "the reserve," any sensible person would turn back to the first page and see "Reserve Fund, £1,450,000; Insurance Fund, £1,311,000." You can judge of that as well as I, but I cannot conceive any sensible person who was inquiring "I wonder what the reserves are" who would not look back and say: "Oh, I see they have got in the reserve a million and a half, and an insurance fund of £1,300,000; that means to say there is on the face of the document a reserve of nearly three million pounds." You will find, as the Attorney-General has conceded at once, and I am greatly obliged to him, that as a matter of fact it is absolutely true those reserves had grown.

The ATTORNEY-GENERAL—I had better make it plain. Far be it from me to mislead you and land you into difficulties hereafter. What I meant to say was that I conceded that, as between 1911 and 1927, the 1927 reserves were larger than the 1911 reserves. I did not mean anything more than that.

Sir JOHN SIMON—No, Mr. Attorney, you and I are never likely to misunderstand one another. Do not let me mislead anybody. I quite agree the point which the Attorney-General keeps for your consideration is this, as far as published reserves are concerned, but I find it a little difficult to visualise the state of mind of anybody who thinks that the statement immediately preceding "Adding to the reserves" does not mean that the reserves are greater at the end than they were at the beginning. If anybody is in that state of mind, I should recommend him to look at five words on the line immediately above: "During the last seventeen years" I read that in this way: "During the last seventeen years every one of those dividends has been paid, after paying the preference stocks, and all the previous charges; and during those last seventeen years we have not only depreciated, and indeed very strongly depreciated, the fleet, but we have also added to our reserves." And that is absolutely, literally, and practically true. If you look at document 105 in columns 3 and 4 there it all is; you get this whole story to the reserves. The columns are headed "Increase in published reserve funds, Reserve Fund, and Insurance Fund," and there you have the story, not a very discreditable story, I should have thought, for any great business, because what it shows is this. It shows that even in very difficult times, when many people with less prudence would most undoubtedly have held their hand, they were going on year after year in that column headed "Insurance Fund" paying in—in 1921, £172,000; in 1922, £74,000; in 1923, £80,000; in 1924, £38,000; in 1925, £40,000; in 1926, £44,000; and



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in 1927, £10,000—with the result that the figures are absolutely as stated. And there is an addition; it does not happen to be precisely fitting, I think, what is stated on the balance sheet, because that does not happen to be the way in which the years are allocated, but it is substantially the same, showing in fact that there has been an enormous increase. Then, says the Crown: “Ah, yes, but there are two kinds of reserves.” Now this is a very funny thing. In one part of the case it is supposed to be most improper, and, indeed, almost criminal, to have these secret reserves tucked away which are drawn upon from time to time; but when it comes to a question of whether you have got reserves, and whether they have grown or diminished, one matter which is considered is the question as to whether or not anything has been done about it. Well, what is the fact? The fact is, if you take the unpublished, the internal, reserves, that in 1911 there were not any.

It is quite true that the peak of the internal reserves had been passed before 1927. The real truth, of course, is that the way in which the dividend had been maintained in these years of difficulty had not been by excessive drawing upon the published reserves, but by drawing on other and internal reserves. The only drawing on published reserves was £200,000 in 1914, and £150,000 in 1926, and the one in 1914 was paid back the next year. The way in which the dividend was maintained in the later years is not by drawing on the published reserves, but, on the contrary, it has been done by drawing from these other and internal resources, and what on earth it is supposed should have been done in this prospectus about it I have very great difficulty in understanding. If it is conceded that it is proper to have internal reserves, that it is proper not to announce how much they are, that it is proper to equalise your dividend, is the proposition then, that if you publish a prospectus, you must tell people that? That cannot be so. The real truth, of course, is that this prospectus is a statement, and it is a perfectly accurate statement, about the reserves of which the prospectus speaks, and every sensible person, man or woman, looks to see: “Now, I have to lend my money to these people; have they got a reserve?” And when you get a reserve fund and an insurance fund standing at these figures, and you are told that the fact is that these reserves have been increased during the past seventeen years, you usually do not imagine that they have only paid the dividends by reducing the reserves to nothing; and when you have done that you have offered a piece of information which you were entitled to offer to the investor.

Now, members of the jury, I have taken longer in opening the matter than I could have wished. No doubt there are other things to which reference might be made, but my submission to you is this—and I make it with great seriousness and invite you to consider it from this time on—I submit that the fair examination of the evidence already given in this case should satisfy any sensible body of men and women that, as matters stand, the Crown has completely failed to establish this criminal charge. What the Crown has done in this Court and in this case is the thing, I

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trust, which the Crown in England will always do, for it is a great tradition, a tradition of the prosecutor in this country. There are some countries where the barrister for the prosecution is all out to gain what is called a victory. There is no victory in this business except in getting justice done. Whether you have previously been in Courts of Justice matters not, who holds office matters not, what party is in power matters not, the one object of those who prosecute for the Crown in this Court is to bring out the facts. There is no contest between my friend and myself about that at all, and it is only just to Sir William Jowitt to say that when he began to appreciate that there might possibly be some misunderstanding about this excess profits duty it was he who carefully went through the figures to make sure that you had the material before you. The only part that I have played is to try to bring out, as is my duty, the result, as I conceive it, and present it, of these figures, and then to call before you Lord Kysant. I am not going to burden you with many other witnesses, because if the case proceeded to its bitter end, I have no doubt it would be more proper that Mr. Morland, of Price, Waterhouse & Co., through his distinguished counsel, should put before you the evidence of a body of accountants, who, no doubt, if it is found to be necessary, will be able to explain these matters to you with a professional authority in the realm of accounts which, of course, I do not profess. But, after all, this has got to be judged by sensible men and women, and I submit to you it is quite clear that nobody pronouncing on this grave issue as to whether or not there has been falsity in the statement of that profit and loss account, or in that prospectus, would take the responsibility of saying: "Yes, I am satisfied that there has"; still less would he go on to say that these false pronouncements had been made deliberately and consciously with the knowledge that they were false and with the intention to deceive.

## Evidence for the Accused Lord Kysant.

OWEN COSBY PHILIPPS, BARON KYLSANT of CARMARTHEN, examined by Sir JOHN SIMON—I am a Grand Cross of the Order of St. Michael and St. George. I was made a peer in 1923. I was born in the year 1863. I began my experience of the shipping business of Britain in Newcastle-on-Tyne in the year 1880. In 1886 I accepted a position in Glasgow, and in 1888 I formed the King Line, Ltd., and acquired my first steamer. The King Line is still in existence and I am still its chairman. I came to London in 1902, for business purposes, and in that year I was elected a director in the court of directors of the Royal Mail Steam Packet Company. Afterwards I came to be chairman of that company. I am still chairman, but I have been given leave of absence by the voting trustees. I was M.P. for Pembroke Burghs, and afterwards for the City of Chester and for the Chester division.

## Evidence for Defence.

Lord Kylsant

I am now Lord Lieutenant of the County of Haverfordwest, Vice-Admiral of North Wales and of the County of Carmarthen. I was appointed president of the Chamber of Shipping of the United Kingdom, president of the Chamber of Commerce of the British Empire, and I have served on a number of public enterprises of all sorts. During the war the R.M.S.P., with its associated companies, placed the whole of its resources and great fleet at the disposal of the nation, and their vessels were very hard worked. The company lost in hostile action something over 100 vessels, and those vessels had to be replaced when costs of construction were abnormally high. The R.M.S.P. made great responses on the subject of War Loans and the like. When the war was at its height, and the arrangement was made about obsolescence allowance I was one of the representatives of the shipping world who negotiated it. It was a very important matter for a shipping company like mine to get a proper allowance from the Government for the building of ships and the postponement of their repairs to a later date. When the war was over, in 1919, one of the results of the Treaty of Versailles was that a very considerable number of merchant vessels became British and the Government did not want ships; it wanted money. The Government of that day appealed through Lord Pirrie to Lord Inchcape and myself to know if we would take the responsibility of those ships, and we agreed to do so on condition that there should be no commission or profit of any sort. The R.M.S.P. got left with a good many ships. Among the lines which the R.M.S.P. has developed and still maintains, there is a very important line running between Southampton and South America. In recent years, South American trade has been exposed to severe competition. In passenger service we have had very keen competition from the Vestey Group, who built five passenger vessels. That other British competition became very severe from 1924 onwards. The Trade Facilities Committee assisted by guaranteeing the building of some vessels, which were used for trading to South America. The same body also obliged by assisting competition and giving guarantees to the competitors.

So that the British taxpayer has been engaged in financing competition?—Yes.

Now, I just want a word about the United States—a country, I believe, which tries to run ships. Take the case of the Pacific Steam Navigation Company—your “100 per cent. company”—it carried on regular services to New York and Valparaiso, and did the United States Government give a great subsidy in connection with this particular trade?—They gave about ten thousand a voyage to the American ships that ran against us.

Then again, the United States Government had a fleet built since the Armistice, and they also operated in various fields?—Yes, they built four large vessels, costing about £5,000,000 sterling, which were faster than the boats of Lamport & Holt—one of the R.M.S.P. group—and when they had lost a lot of money trading with them they sold them to the managers for under a million sterling and gave them an enormous subsidy for running.

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In those circumstances, with keen competition against a British line, is it in your view in the interests of the company, and those who are shareholders in it, to announce in detail the state of your own trading affairs year by year?—No.

Assuming that you were for some years doing badly in trade, it would manifestly stimulate competition, and in any case it would give competitors a great deal of information?—Yes.

And has that view of the matter in your time been recognised by the board and, as far as you know, by the shareholders?—I think every one who has much to do with shipping recognised that.

Would you regard it as injurious to the interests of the shareholders if elaborate details were exposed?—Yes.

Are you, yourself, a believer in what is sometimes described as the shipping trade cycle?—Yes.

And without professing to explain exactly the economic cause, do you believe it to be confirmed by the experience of British shipping?—Yes, in my fifty years' experience it has varied between seven and ten years before you got to the peak. In 1906 there came the crest of a wave. That time the length of the cycle was only six or seven years. Another cycle of about six years followed, which brought us to the crest of a wave in 1913, and then there came the great war.

In the year 1914 your company paid no dividend at all?—No, the Royal Mail did very badly.

When you come to 1919, you get great activity and the crest of a wave in 1920?—Yes, it was in the spring of 1920.

19th March, 1920, was the date of the Budget statement of that year, and there is no doubt at all there was a sudden increase of taxation and a very sharp decline?—Yes. The years 1921 to 1925 showed results which could only be considered as below the crest of the wave, some of them seriously below. The company's accounts came before the court of directors at each meeting, and were examined with the corresponding figures of the previous years.

So that not merely you, but every other member of the court of directors had them before them?—Yes, and they were attached to the minute book so that each member could read them.

Is the statement in your report true that, in the first four months of the year 1926, there was a considerable increase, in your group of companies, in your export trade?—Yes.

Applying to that situation your past experience and belief in the cycle of the shipping trade, did you form a view as to whether in the next year things would improve?—I hoped that when that year was over the following year would begin on the up grade.

The general strike had a seriously depressing effect at the time?—Yes, very, and no one could say how long it would last.

In 1926, notwithstanding the general strike and other circumstances, there was an increase in the earnings of the fleet, and the deficit was smaller, so that when we come to 1927 there was a substantial further improvement. In 1927, was it your view that things were improving or growing worse?—Improving.

## Evidence for Defence.

Lord Kylsant

Did you regard that as confirmed by considerations of the shipping cycle?—Yes.

Was that view very widely held in business circles?—That was my view I believe so

It is obvious that we can all be very wise after the event. Now I want to ask you as to the practice which, under your guidance and advice, the court of directors followed in the matter of seeking to equalise dividends. We see, of course, on the figures what, in fact, has been the course which has been pursued. In your view is that a prudent, business-like course?—Yes

It involved, for instance, going back to the beginning of the period mentioned in the prospectus. The distribution of dividends was 6 or 7 per cent., whereas it would have been possible to have distributed 13 or 17, or whatever it might be?—Yes.

Is it in your experience a recognised practice—this method of endeavouring to equalise dividends in well-managed shipping concerns?—Yes.

I suppose, in fact, the position fluctuates a good deal?—Yes.

There are a hundred things to consider: currency and exchange, and so on?—Yes.

Had that policy the approval of your court of directors?—Entirely.

That involves, as we realise, the setting aside of some reserves?—Yes.

Is it a fact that the reserve fund—the published reserve funds of the R.M.S.P.—was increased and added to as between 1911 and 1927?—Yes.

Continuously?—Practically continuously.

Is the existence of large published reserves, such as we see in your balance sheet, an important consideration as security for those who are invited to lend money to the company?—Yes.

You say on one page of the prospectus, after the statement of the capital reserve fund, that there is a reserve of £1,450,000. Do I understand rightly that the insurance fund, being in fact in excess over the claims upon it, is really also a reserve?—Almost entirely a reserve. Almost the whole of it. My practice has always been to debit more for insurance than it actually costs.

Having stated the reserve fund on the front page, you got a statement on the second page, “adding to the reserve and payment of dividends.” Is it true that the reserves have been increased as between those years?—Yes.

I understand that apart from that and quite outside the published reserve, to which attention is called here, there were in addition some internal reserves?—Yes.

Did you see any objection at all to the reservation of an internal or secret reserve?—No.

Is it in your experience a part of the ordinary management of great businesses of this sort?—Yes.

If there is going to be an internal reserve, is it, in your view, in the interests of the shareholders that you should publicly announce

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how much it is?—No. My view is that it is to the advantage of the company not to publish them.

I suppose the reason they are internal or secret is that they were not published? Your shareholders have shown every confidence in the board, but is it the experience of directors generally that if it were shown there were great sums available the question then does arise: "Then why should not more be distributed"?—Yes.

And does it not follow that the existence of a reserve is a resource against a rainy day which, in the interests of the company, you do not think it advisable to announce?—Yes.

If there is further or published reserve, that is additional?—Yes.

Now, when one looks at the figures we see that the way in which in the later years these dividends were maintained was owing to the circumstance that there were internal reserves to which recourse could be had. I notice, as a matter of fact, that you did not seriously deplete the published reserves at all?—Except that one year—the general strike year.

Look now at the statement in the prospectus with regard to the R.M.S.P. Company's satisfactory position in spite of the general trade depression. You are responsible for making that statement, and you understood the matter. Is it true?—I am not the only one responsible, but all my colleagues.

But I don't suppose you are shirking it?—Not in the least.

I must ask you the question, is it true?—Yes.

And in the same way about adding to the reserves, is that true?—Yes.

Let us suppose for a moment that somebody could pick holes in the statement. I am not saying they could, but just suppose they could. Did you ever know that it was untrue?—No.

So far as you are concerned, had you ever the smallest intention of putting forward a statement that was not true?—No.

Had you ever any intent to deceive or defraud any member, shareholder, or creditor in the matter at all?—No.

One other phrase I must put to you, and I do it with great solemnity, because your answer is one on which much may depend. Supposing again that somebody could pick holes in this prospectus, were you ever a party to making a statement in this prospectus with intent to induce persons to become prospective subscribers by means of false statements?—No.

Is it a fact that your board, as a rule, got a fairly full attendance of its members?—Nearly always. There were four or five members, and they nearly always attended.

Did you keep internal reserves a secret from the meeting?—No.

Or was it a fact that they knew?—They knew as much as I did.

Tell us what happened when the accounts were discussed?—When they came before the court of directors the chief accountant came into the room. I took the sheet and went through every item on one side of the balance sheet, and then I went to the other side and went through

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every item and made remarks about them, and then did the same about the profit and loss account.

As I follow you, the other members of the board would be studying the voyage accounts from month to month?—Yes.

So a general view is gathered from that?—Yes.

This is not material to the charge, but so far as you know, have you ever misled or overborne the board?—Never.

These voyage accounts, I imagine, from time to time, in later years would show deficits as a matter of trading?—Sometimes heavy deficits.

When it was observed that the recent reports of the voyage accounts indicated heavy deficits, did the question arise as to how the losses could be met?—That was one of the things that were always discussed.

And such things as E.P.D. and other reserves would be very useful?—Very useful.

One more matter with regard to the profit and loss account. Part of the profits from the actual trading would arise from the actual shipping business, but, quite apart from that, had the company very large investments?—Yes.

Investments in the 100 per cent. companies and also in companies in which you did not hold a 100 per cent. interest?—Yes.

I will just mention one or two of the more important. Take, for instance, Elder Dempster, which is not a bad example, representing £440,000 in your books. Then Coast Lines, Ltd. What is Coast Lines? Where do they go?—They go nearly everywhere on the coast.

I will give you another name. The Argentine Navigation Company?—That was a company that we bought during the war. The Government gave us permission and we bought it from an enemy alien, an Austrian. I would like to say we bought it by permission of the Government, up to 60 or 70 per cent. We bought it at par at £1 shares, and the shares were quoted on the Stock Exchange at 4s. 6d. We stuck to it, a change came, and when the voting trustees were appointed a year ago they asked me if I proposed to sell. I said I was sorry, but I couldn't do so, and then we sold at 25s. after their going down to 4s. 6d.

And as to the 100 per cent. subsidiaries, are the reserves something like £12,000,000?—Yes.

Now coming to the profit and loss account, look at the account for December, 1926. As a matter of fact this expression, "adjustment of taxation reserve," was not invented by you?—No it was Mr. Morland who thought that was the proper phrase to use.

As far as you know, was it perfectly proper?—I think so, but I am not an accountant.

So far as you understood at the time or understand now, is there any statement whatever which is made in the profit and loss account there which is false?—Nothing whatever.

If anybody could pick holes in anything, was it to your knowledge false?—No.

In putting forward the profit and loss account, did you ever have any intent to deceive, mislead, or defraud?—No.

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Do the same answers apply to the corresponding documents of 1927?  
—Yes.

As a man of great affairs and with inside knowledge, have you ever speculated in shipping shares?—I have never sold a shipping share in my life. I think in one small family trust company, twenty-five years ago, I sold 20,000.

Right or wrong have you regarded it as one of your opportunities and duties to try to maintain the prestige of British shipping in the face of the competition of the world?—Yes

And standing there, on your oath and on your trial, are you aware that you have ever failed in the discharge of that or of any other duty in connection with the company and its shareholders?—No.

The Court adjourned.



# Evidence for Defence.

Sixth Day—Monday, 27th July, 1931.

LORD KYLSANT, further examined by Sir JOHN SIMON—In your experience, both in connection with the Royal Mail and allied companies and generally, is so large a rate of depreciation as 5 per cent. really necessary, or is it excessive?—I consider that it is not necessary and excessive, but it gives the advantage of an internal reserve without talking about it.

Such a rate of depreciation as 5 per cent., instead of 4 per cent., over a series of years would give an internal reserve which would eventually become a very large figure?—On the Royal Mail group, many, many millions.

In the instances we have observed, when a ship came to be sold for any reason, it appears to have realised more than its book value?—In nearly all cases.

Is there any exception to that?—There was one just after the war. In 1930 there was one. We had to buy a ship to carry on a certain trade—the “Oruba.” We bought her for £175,000. We ran her two or three passages, but she was quite unsuitable. In the first four years we wrote off 50 per cent. depreciation, and then sold her to be broken up for a nominal sum, and we charged profits on the year with the difference of about £70,000.

Cross-examined by the ATTORNEY-GENERAL—You are a director of a very large number of companies?—Very few, except the shipping group.

A very large number of companies altogether?—I look upon the shipping group as practically one, although there were 35 companies. Apart from those companies I am a director of only four or five concerns.

Your experience in the City of London in connection with companies is considerable?—It is considerable.

You are, or were, a director of one of our great banks, a director of one of our great railway companies, a director of an insurance company, a director of an investment company, and a director of shipping companies?—Yes.

Do you agree that the primary function of a balance sheet is to show the true and correct view of the company's affairs?—I should say it certainly was to show the true and correct view of the company's affairs.

When I talk about a balance sheet, I include the profit and loss account, since the one is always connected up with the other?—They should certainly both be true and correct.

That is the primary function, and all rules of accountancy are merely subsidiary towards that end?—I do not know much about accountancy.

With regard to internal or secret reserves, would you tell me from your experience that it is a common thing for internal or secret reserves

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to be built up?—A certain number of internal reserves are good for all businesses when they can have them.

In this case, I have not in any way questioned the propriety of so doing?—I agree.

Next, you tell me that internal reserves which have been built up may, with propriety, be used to level out the inequalities of one year with another?—That is my view.

That is done?—Yes, it is done.

I hope you will observe that I have not questioned in any way the propriety of doing that. If you have a temporary exceptional loss, of a temporary character, if you call attention to that, you might, so far from reproducing a true and accurate view of the company's position, give a false impression of the company's position?—Yes, I agree

However good the principle may be, nearly all principles can be misapplied, can they not? You would agree that the extended and continuous utilisation of large sums drawn from secret reserves, without any indication, at length becomes misleading?—It could, under certain circumstances

I will adopt a very neutral phrase It has been said: "There would come a time when the auditor would say: 'Now, if these reserves are to be used again, some indication must be given to the shareholders that the profit and loss account is augmented by transfers from the E.P.D. or other reserves.'" Would you agree that there does come a time when some indication must be given?—There might come a time

Supposing that time comes when indication is necessary, the indication must be sufficient, must it not, to turn something which admittedly without it would be untrue and inaccurate into something which is true and accurate?—I feel that that is a question which a chartered accountant could answer better than myself.

I want your business sense of it, and your great experience We agree that a time might come. We are not discussing whether it has come in this case, but a time might come when an indication ought to be given to the shareholders of the utilisation of secret reserves?—It might come, I agree.

Assume, in a given case, such a time has come On that assumption do you agree that the indication which must be given to the shareholders must be a sufficient indication to turn something which would otherwise be untrue and inaccurate into something which is true and accurate?—It is all a question of assumption. If it is a question of law, I always get the very best opinion which is available in this country. When I am dealing with accounts, I try and get the very best opinion of accountants I do not set myself up as knowing anything about law or knowing anything about accountants' work. I want to be quite frank. This great company, or group, has had five great lawsuits in the last ten or twenty years. We have won every one of them. That was not because I knew anything about law, but I always instructed our solicitors to get the very best opinion there was, and I try to get the same with regard to accounts.

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I only wanted to get the business sense of a very experienced business man. Assume, if you will, that a time has come when some indication must be given to the shareholders; it must, in your view as a business man, be sufficient to prevent the balance sheet being false and misleading?—I should generally agree with that

Come to the actual case of your company. It was in the year 1925 that the words about adjustment of taxation reserve were first used. It is a matter of history?—Yes.

Do you agree with me that the circumstances which existed in 1926, having regard to the previous history, were such as to make it necessary that an indication should be given to the shareholders if you were going to draw further from the secret reserves?—The court of directors did make a direct indication to the shareholders by drawing £150,000 from the open reserves, and therefore had drawn, in my opinion, the attention of every one to the fact that the general strike of 1926 had hit practically the majority of the great companies in the City of London.

You are answering the question by inference. Do you agree that by the year 1926 a situation had arisen which necessitated an indication to the shareholders?—No, I do not.

Do you really mean "No"? A moment ago you told me that an indication had been made, and done for that purpose. I am not sure that you follow it, and you should not answer any question without following it plainly. Do you agree that, in respect of the year 1926——? —Do you mean by the year, or in respect of it?

I mean in respect of it?—I was answering by the year.

I mean the accounts which are actually signed and published somewhere in May, 1927. Those accounts are in respect of the year 1926. Would you agree that the time had come then when an indication had to be given to the shareholders?—I do not agree that a time had come, but at that time an indication was given to the shareholders of that particular year, not because one hundred years before or fifty years before——

We both agree that the accounts in respect of that year had to give an indication to the shareholders?—I agree.

Do you agree that in the absence of an indication to the shareholders these accounts would have been false and misleading?—They would not have been false and misleading.

Look at the profit and loss account for the year 1926. There were certain items referred to as "special credits." The M.P.D. reserve was, as it were, part of the vintage of the years 1918 to 1920. It was then the grapes were harvested, picked, pressed, bottled, and stored in the cellar. But the bottles did not become drinkable until the year 1926. For the first time it became possible to drink that £550,000. That metaphor expresses what was the case?—I think it is rather misleading.

There has been confusion here regarding free reserves and old reserves. They were old reserves. Your case is that they first became

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free in the year 1926. That I understand to be your case?—I do not accept the position.

I will pass from this point. At any rate let me call them exceptional items. There were brought into that account an exceptional and non-recurring item?—They came in that year.

There are the words “adjustment of taxation reserve” Do you attach any, and if so what, importance to those words?—Those words were not suggested by me. I saw no objection to them. I do not go further than that. The big item was, in my view, the earnings of the company in that year.

I am asking you, as a very experienced business man, whether you attach any, and if so what, importance to these words “adjustment of taxation reserves”?—I do not attach much importance to them.

Equally, may I take your view to be this: the ordinary intelligent man in the street, the investor, the shareholder, he also would attach little or no importance to these words?—No, I do not go as far as that. You ask me whether I, as chairman of the company, was satisfied that the published statement that we had drawn £150,000 from reserve—

I ask you, having told me your view as chairman—I ask you to tell me whether in your view the ordinary investor would attach any, and if so what, importance to these words “adjustment of taxation reserve”?—I could not answer that. They attach great importance to the other point.

Did you anticipate, or did you not anticipate, that the ordinary investor would attach any importance or significance whatever to these words “adjustment of taxation reserves”?—I think naturally he would attach some importance.

What importance do you think he would attach to them?—I am not qualified to answer that.

Would you have attached any importance to them?—I should have attached some importance to them.

What importance would you have attached to them?—You are asking me questions which would be much more suitable to be dealt with by accountants of some description.

If you will forgive me, that is exactly what I am not doing. I am seeking to consider the effects of these words on the ordinary man in the street, and not the technical meaning. I asked you to tell me whether you, yourself, would attach any, and if so what, significance to these words?—If you put it that way, I should say I should certainly attach some significance. As to the extent to which anybody else might attach significance, I am not really in a position to answer.

Are you able to explain to me more nearly what significance you would attach to them?—I should attach to them what it states—that there was an adjustment of taxation reserves.

Look at the profit and loss account for the year ended 31st December, 1926. You see what you told the shareholders. You told them quite plainly, in capital letters, that you were transferring from the reserve fund £150,000?—Yes.

The shareholders would know, by looking at the balance sheet, that

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after the transfer the reserve fund was £1,450,000, and would also know that before the transfer the amount was £1,600,000?—Yes.

All that you tell the shareholders quite plainly?—Yes

You never told the shareholders, did you, or where did you tell them, that you were bringing into this year's balance £550,000 from the E.P.D. reserve?—I do not think it is exact to say it is being brought in from the E.P.D. reserve. I think it only became available in the year 1926, which is an entirely different proposition.

Let me accept that. Let us assume that you were bringing in an entry from an E.P.D. reserve to the extent of £550,000, which only became available that year. Where do you tell your shareholders that?—We have never told them how the balance of profit and loss is made up.

I quite agree, but you have told me that in respect of the year 1926 it was right and fair and proper that the shareholders should have an indication?—That we were passing through a difficult period.

Bearing that answer in mind, where do you tell your shareholders in this document that you are making use of a credit from E.P.D. reserve, which credit had become available for the first time that year?—There are two things. There was the transfer from the open reserve and the addition of the words "adjustment of taxation reserve." I think that fairly covers the point.

It certainly is not in the transfer of £150,000?—You must take them together.

You can leave that out, as far as the £550,000 is concerned?—I should not go as far as that.

Do you mean to say that the shareholders would have an indication of the fact that £550,000 credit was being made use of by reason of the fact that you say "transfer from reserve £150,000"?—You take the two things together. The £550,000 came into the company for the first time that year. Taking the two things together, I think it was a fair statement and an accurate statement of the company's position.

You say that the shareholders get that indication from the words "adjustment of taxation reserve," coupled with the words "transfer from reserve fund"?—Yes.

Any shareholder looking at the balance sheet might say that the company was paying 4 per cent. as the dividend on its ordinary stock. The dividend had been 5 per cent., but it had fallen, and there had been a transfer from reserve of £150,000. In your view would there be anything in that document to cause any alarm to the shareholders?—When shareholders saw that the dividend had fallen from 6 per cent. to 5 per cent., and then to 4 per cent., they were naturally concerned.

The only thing which would occasion any alarm to the shareholders in connection with the profit and loss account was that the dividend was now 4 per cent., whereas the year before it had been 5 per cent., and the year before it had been 6 per cent.?—Yes.

And nothing else at all?—Coupled with those two things. You cannot only take one part. Coupled with the fact that there was drawn £150,000 from the external reserve, and the remark "adjustment of taxation reserves."

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I chose my word "alarm" with some care. In your view, leaving out the rate of dividend for the moment, was there anything in this document whatever which would cause any alarm to the shareholders?—My personal view is that, beyond the facts stated, there was nothing, either in the document or in the business, to cause any alarm to shareholders.

There is nothing in this document, in your view, to cause any alarm to a shareholder?—Except that the profits were going down for three years running.

That leads me to ask you a question or two about the business itself. The year 1920, you told us, marked the crest of the wave, and was the end of the boom. The year 1920 particularly had been a very satisfactory year?—Yes

You were wisely and prudently putting aside in the year 1920 for the future interests of the company. You put aside special debits of over half a million in that year?—Yes. They were to meet special liabilities. It was not the setting aside a large sum without expecting liabilities. It was provision for expected liabilities.

In the year 1921 there was a deficit of £450,000, and there was brought into the profit of the year £1,120,000 by way of special credits?—They were bonuses reserved from certain companies. I do not agree that those bonuses were in the nature of non-recurring items. A big company has many non-recurring items.

They were bonuses paid by companies and represented earnings over a period of years of those companies?—Some of them.

Look at the balance sheet. It states "profit for the year, including dividends on shares in allied and other companies, less depreciation of fleet." The deficit in the year 1923, after credit for investments, was £20,000?—I should like here and now to say that I have never seen the document which you are reading before. I am not responsible for the way it has been made up, and I do not know personally that the figures are correct. The way it is made out, quite frankly, is grossly misleading.

I do not seek to hold you responsible for the way the document was made out. Does it show that in the year to which I have just referred special credits of £800,000 were brought into the accounts?—I see that figure in the document.

If you turn to the profit and loss account for the year to December, 1923, you see that the word "profit," as it was before, has now become "balance" for the year?—Yes.

Why was that? Do you know, or was it an accountancy question?—It came before me. Whenever a thing comes before me and I find it is strictly accurate I agree to what is suggested. I always agree at once. That is my business principle. We do not publish a trading account, and directly my attention was drawn to the fact that "balance for the year" was more strictly accurate than "profit for the year" I approved at once.

What is the exact significance that you attach in your mind to

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the distinction between the word "profit," which had been the word used hitherto, and the word "balance," which appears in 1923 for the first time?—When I became chairman, twenty-seven years ago, the company had a capital of £900,000, but it has grown bigger, and has received its revenue from a large number of sources, and the original way of talking of a profit for the year was misleading and inaccurate. Directly my attention was drawn to the fact that it was more accurate to say "balance for the year . . ."

My difficulty is, why do you think "balance" is more accurate than "profit"?—Because it is not a trading account. If it had been a simple company owning 20 or 30 steamers, and the result of the year was simply the profit on voyages, a profit and loss account would have been a trading account, as it was originally.

Do you think that a shareholder would have attached the slightest significance to the alteration of the word "profit" to "balance"?—I think so, personally.

You do?—Yes, I do. I should have done it a few years earlier if my attention had been drawn to it.

The deficit in 1924 is shown at £97,000?—Yes.

And the special credits are £870,000; that is to say, roughly £800,000 in excess was brought into that account?—Yes.

Let us look at the years 1921, 1922, 1923, and 1924. In each of those years a dividend of 6 per cent. on the ordinary shares was paid?—Yes.

The amount required in 1923 and 1924 to satisfy the debenture-holders was £218,000?—Yes.

Although it is right to say that you have told us that depreciation was on the generous side, yet it is a fact that in every one of those years there was a deficit before you had paid the interest on the debentures?—I should have to look into that. I cannot answer that sort of question. As chairman of the company, on questions of policy, I recommended to my colleagues as to what they should decide. The actual form of the accounts is drawn up by the accounts department, and they submit recommendations.

You told me, when I was dealing with the year 1926, that there was no need for any shareholder to have any alarm?—Yes.

I am looking at the history of the company to see whether there was any need for any shareholder to have any alarm. I am taking four years, 1921, 1922, 1923, and 1924, and asking you this: Bearing in mind your point with regard to depreciation, and subject to that, is it right to say that in every one of those years there was a deficit before you had paid anything in respect of your debenture interest?—The charge for debenture interest comes on the company before depreciation. There had been enormous sums allowed for depreciation. You pay debenture interest before providing for depreciation.

Take the year 1923, which is the one with the smallest deficit. After the interest on investments comes in, this table shows a deficit of £20,000. I am suggesting that that deficit of £20,000 is not arrived at after

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including the payment of debenture interest, but you have got to pay your debenture interest of £218,000 on the top of that deficit?—I am being asked questions on a document I have never seen before, and there are figures with which I do not agree.

I am pointing out to you that, subject to your depreciation, in every one of those years from 1921 to 1924, there was a deficit even before you paid your debenture interest?—I think that is a very misleading way of stating the facts, grossly misleading, in my opinion.

In those four years did you consider that the company was getting into serious trouble?—No. From 1925 up to 1927, things were steadily on the up grade, although they were moving slowly.

Were things going well with the R.M S.P. in the years between 1921 and 1924?—They were going in a normal way for shipping in difficult times. Things were, of course, on the down grade. After 1924 difficulties in connection with the business became more serious, particularly in regard to competition and competitors. The United States Government were subsidising shipping.

You can go farther than that and say that the French Government started to subsidise?—It was very difficult to find from the French finances what they were doing. I understood that for some years after the war, when they were not paying us any interest on our loans, they were simply handing over to every shipping company sufficient every half-year to pay a 5 per cent. dividend and any losses they had. It did not appear in the Budget of France.

As from the end of 1924 this was the situation; the volume of goods to be carried had shrunken very considerably as compared with the end of the war?—I could not answer that question on the particular years now.

There did come a time when the volume of traffic fell off. The volume in 1920 was abnormal?—Yes.

And that abnormal situation had ceased to exist by 1924?—Yes.

From 1924 onwards was this the situation, that there was a quantity of tonnage available to carry goods far in excess of the volume that required to be carried?—I could not answer that question without reference.

Give me your impression as a great shipowner. Am I saying anything that seems unlikely when I state that from 1924 onwards the available quantity of shipping was far in excess of the volume of goods required to be carried?—After the war we were first very short of tonnage, and then there was a great increase of tonnage which was built. So far as 1924 is concerned, I would like to look up the facts.

At any rate, the situation prevailing round about that time was a totally different one from that which prevailed just after the war?—Yes.

That becomes important on another branch of this case. Will you tell me why you say this table to which I have referred is grossly misleading?—I cannot question the accuracy, but I feel that it is a table on which you could cross-examine any chartered accountant or our heads of finance. They could deal with it. I have never seen it.



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This table or document shows the build up of the balance sheet?—I am not disputing that, but you are cross-examining me about a thing I have never seen before.

I don't want to wrangle with you, but you tell me that you have not seen the document, and cannot be responsible for the make-up?—That is so.

What you said went much further. You said that the document is grossly misleading. Why is it misleading? What do you say is wrong about it?—We decided what we shall write off for depreciation. There have been enormous sums for depreciation. In 1926 there was £626,000 for depreciation.

That was the figure you charged in your books?—After we had considered the accounts. The profit and loss account, if we had not made these internal reserves, would not show the debit balance, as you call it.

Taking the years 1921 to 1925 together, the special credits brought in exceed the special debits by approximately £1,000,000. That is only a matter of arithmetic, and it shows that during those five years the company was carrying on business and living on the reserves which it had previously stored up. Is that true or untrue?—I personally think it is untrue, for this reason: the fleet of the group was standing at about £5,000,000 or £6,000,000 less, having been written down that amount, partly in those years. From 1911 to 1927 the reserves increased by £2,231,000. You should bear those facts in mind.

As against that, you should bear this fact in mind, that in each of those years there is a large sum which represents interest on investments?—Yes.

The companies paying that interest were, to a large extent, themselves paying their dividends out of reserve, which they in their turn had stored up?—In some cases, certainly.

Take an instance of where you were chairman, the Pacific Steam Navigation Company. It would be right to say that the Pacific Steam Navigation Company had never made a profit, after depreciating, since 1921? Do you know that?—No, I do not. It certainly has made some very good profits before providing for depreciation.

Looking at the accounts for the year 1925, you see the words "adjustment of taxation reserves"?—Yes.

Would you have regarded that account as a fair and accurate account without those words?—I should not have thought it was absolutely necessary, but when it was pointed out to me that it was desirable to have them, I agreed, because any amounts received during the year which were credited were sums that appertained to the year.

Do you think, if you had published the full facts to your shareholders at the end of 1925 as to the results of the five years' trading, that there would have been a panic?—No, I do not think there would have been a panic.

It has been said that one of the reasons justifying the use of internal reserves is to avoid disturbance. Do you think, if at the end

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of the year 1925 you had published the facts of that year, that your shareholders would have been seriously disturbed?—No, I think that if I had published the full facts for every one of these years you have been talking about, the shareholders would have been agreeably surprised.

I am not talking about the group of companies, but of the Royal Mail Steam Packet Company. You think if you had published the full facts the shareholders would have been satisfied? I understood it was one of the main justifications, from the business point of view, for the utilisation of internal reserves, that it is to avoid fluctuations of shares and shareholders being disturbed?—Yes.

Do you really tell me and the jury that if the facts as they existed at the end of 1925 had been made public, the shareholders would not have been seriously disturbed?—No, if it was made public exactly how much was written off for extra depreciation and how much not only the R.M.S.P., but its 34 other companies had reserved, I think they would have been agreeably surprised. That is my candid opinion.

As a hard-headed business man, do you tell the jury that the shareholders would not have been disturbed if they had known all the facts?—If they had been published in the way that they are set out here. But if the full facts of the Royal Mail, the 100 per cent. companies, and the group had been published, there would have been nothing to disturb anybody.

If the shareholders had been told, "This year we have made no profit at all; we cannot pay our debenture interest out of current profits, but we propose to pay a dividend of 5 per cent." do you think the shareholders would have been disturbed?—This document is grossly misleading. You are talking as if there was a deficit, but the profit on the Nelson Line was £490,000 odd. That should be added on.

We do add it on. That comes in as one of the special credits?—It may come in just as well under "interest on investments."

Whether the shareholders would have been alarmed or not, "adjustment of taxation reserves" was put in, and you assented to that?—Yes.

And do you regard it as being, as it were, a danger signal or an indication?—I do not regard it as a danger signal. I regard it as informing the shareholders of what was happening.

At any rate, after the publication of these accounts for the year 1925, with these words, nobody was in fact disturbed by the presence of the words. Were there any questions asked at any meetings?—I think I had a fair number of questions.

Any questions asked about those words?—No, not exactly. I do not recollect them.

The quotation of the ordinary shares remained steady, both before and after?—I have not got those figures before me.

It has been stated in evidence that when Mr. Cason attended at meetings of the court of directors of the R.M.S.P. there were no discussions regarding the accounts. Is that correct?—No. Mr. Cason was only present in the board room for twenty or twenty-five minutes. If

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what you have suggested is a record of what took place at the court of directors, it is absolutely untrue. I have been looking forward to this opportunity to put the true position forward.

Mr Cason has sworn that, at the meetings at which he was present when the accounts were discussed, no mention was ever made at any of those meetings with regard to these reserves, or anything of the sort. When these matters are discussed, you would have your chief accountant there?—When the chief accountant brings in the accounts to the court, which is held once a year, a month before the annual meeting, the auditors have not passed the accounts. He brings in a full statement, and I go through every item on the balance sheet, first on the one side and then on the other, in full detail.

What balance sheet?—The balance sheet that he has submitted. I then go through every item in the profit and loss account. I answer my colleagues any questions they ask, and if the court thinks that five gentlemen of the experience of my colleagues on this great company never asked any questions or knew about anything—well! I listened to the evidence of our chief accountant with regret, so far as he was concerned, because I felt it was absolutely and utterly wrong. We have the voyage accounts of every company, and I see them every week. The full voyage accounts of the month are submitted to the court of directors, and either I, as chairman, or the secretary reads out the results of each voyage, and then we compare the corresponding voyage of last year, and when you have been through all of them you read out the total, and they know exactly what the company's steamers are doing.

I entirely follow your point when you say that the directors have an opportunity of having the voyage accounts, and from them they ought to have known the position, but what I am trying to get clear is, were there ever in the presence of the accountant any conversations at all?—Yes.

How often?—Practically every year. The statement made was grossly misleading. I regret to have to say so, because I have worked with Mr. Cason for many years. May I say just this? I always motored down to the City with one director. Another director, one of the ablest men on the board, always telephoned to me the night before, and asked to be kindly motored down to the City. Always before the annual meeting he came down on purpose, so that he might cross-examine me into the most minute details of the company's business.

Those directors are still alive and well?—One, I regret to say, has passed away.

And some of them are near or in the City of London, and could easily come to this Court, so far as you know?—Yes.

Now come to 1926. Mr. Cason told us that you had instructed him to prepare a document which he called Exhibit No. 6. Did he show it to you on 12th October, 1926?—Yes.

And this document showed that you had an estimated deficit of £1,100,000?—Yes.

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And that is a deficit without paying anything on the ordinary shares at all?—Yes, that is shown in the document.

Did you ask him what unpublished reserves you had got, and how you could meet the deficit?—Yes.

Then he wrote on the right-hand side, either on this or some other occasion, these figures totalling up to £1,144,956?—Yes.

And under that comes "bonus shares from Nelson's, £200,000"?—Yes. It was decided that the bonus share scheme should not eventuate.

Do you see the figures there making up the £600,000?—Yes.

Do you see the E.P.D. is there placed at £350,000?—Yes.

Do you know that when the Nelson bonus was washed out the E.P.D. moved up another £200,000 to £550,000?—Yes.

Do you really suggest that this is an adjustment of taxation reserves? Is it not simply taking from taxation reserves whatever is necessary to meet the deficit?—No I suggest it is adjusting taxation. I do not use the word "adjusting" in my ordinary business life. It is a professional word.

Supposing that the Nelson bonus had gone through, do you think the E.P.D. would have been adjusted to the tune of £350,000 only?—I understood that there was about £350,000 coming in from E.P.D. returns. It afterwards came out that it was £550,000. I think that is right.

You are not suggesting that is why you left out the Nelson bonus? When that did not materialise, you moved up the E.P.D. figures?—No, it was the other way about. When we found we were going to get £550,000, the directors of the Nelson Line postponed making a bonus until the following year.

In that year you paid a dividend of only 4 per cent.?—Yes.

Did the shareholders know the company was living on reserves?—I do not agree that it was.

Would you regard it as imprudent finance to pay a dividend of 4 per cent. when you are drawing from reserves?—The whole of the circumstances have to be taken into consideration.

If you published the full facts in 1926, would the shareholders be seriously disturbed?—I think not.

Or even disturbed. Do you really mean that?—Yes, absolutely.

The report for that year was well received, was it not?—Bearing in mind that we were drawing on published reserves.

And the quotations of the shares remained constant?—I never follow the Stock Exchange.

In respect of the year, there was a necessity for some warning?—Yes, because it was the year of the general strike, which came about May.

Let us see what warning the shareholders got. There are the words "adjustment of taxation reserves," which would, I suggest, convey nothing to their minds. There is not much other matter to tell them that special credits of £750,000 were being used?—I think you are inaccurate in describing what are called special credits as transfers

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If you had regarded them as transfers from reserve, you would have given a clear note of warning?—I would consider the matter on its merits. They were not transfers from reserve.

Sir JOHN SIMON—One of the figures is £175,000 for income tax. Am I at this stage of the case to understand that the Attorney-General is still going to say that that is a transfer from reserves?

The ATTORNEY-GENERAL—With regard to the excess profits duty, £550,000, I am going to say that is transferred from reserves. With regard to income tax, I am going to say that with the exception of that part of it which arose in the year, which I am going to say is the income tax on dividends paid, roughly, £130,000, that, too, is a transfer from reserves. I am drawing a distinction between old and free reserves. It may well be that the £550,000 only became free that year, but it does not alter the fact that that was an old reserve.

The WITNESS—I do not agree with the view you are expressing. You are asking me on the assumption that what you are stating are facts.

*Cross-examination continued*—I want you to deal with an assumption, if you will. I suggest to you that the £550,000 had arisen in this way, that in the old days, substantially up to and including 1920, large sums of money had been put aside in respect of the liability which was then anticipated for E.P.D.—That is so.

As time went on, it was possible to gauge with some precision how much of that old reserve would be required?—That is one way of stating it. We find out each year what we will get back from the Treasury, and that goes into the accounts for the year.

The reason why money came in in the year was because in the years 1918 to 1920 you had paid large sums of money and you were getting a refund of what you had paid some time ago?—We did not know until 1926 that we should get this refund.

But you did get it?—Yes, in 1926.

And that was a refund of something you had paid a long time ago?—But we did not know until 1926, and when it was refunded it was paid straight into the profit and loss account. I fail to see that there was anything not strictly accurate in doing that, and it was part of the income of the year.

I am not suggesting it is inaccurate, but I am only suggesting that you bring the money in without telling the shareholders what you are doing. I say that that is misleading. I refer you to a speech you made about this matter on 26th May, 1927. Do you see this—

The accounts reflect the abnormal conditions which obtained last year as the result of the General Strike and the prolonged coal stoppage. Whilst indications in the early part of last year pointed in the direction of a general recovery from the protracted depression in trade, all hope of this was frustrated by the industrial troubles which followed. Operating expenses were substantially higher by reason of the extra cost of coal and otherwise, while exports of manufactured goods diminished. As a precautionary measure, the court of directors thought it well, in October last, to refrain from declaring an interim dividend, but, after providing for taxation, debenture interest, and preference dividends, and writing off depreciation on the basis of 5 per cent. per annum from the first cost of the fleet, they now recommend a payment of a dividend on the

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ordinary stock at the rate of 4 per cent. per annum, less income tax. It is proposed that the balance of £66,782 at the credit of profit and loss account be carried forward. The sum of £150,000 has been withdrawn from the reserve fund, which now stands at £1,450,000, whilst the insurance fund stands at £1,300,947. The directors feel justified in making the transfer from reserve seeing that for many years past they have followed the sound conservative policy of paying moderate dividends on the ordinary stock while building up a substantial reserve fund, and at the same time have provided amply for depreciation, not only on the customary basis of twenty years' life, but by writing off additional special depreciation in past years.

There is nothing there to tell anybody that there had been any transfers from reserves over and above the £150,000?—But there was not.

Let me suggest to you that there was a transfer from the reserve of a sum which became free, if you like, in that year, and there was a transfer of reserve in respect of the year 1926 of £550,000 E.P.D.?—I thought we had already dealt with that.

You dispute it?—I disagree with the view you take. I am only giving a business man's view.

Did you discuss these matters with your co-directors?—Yes.

Did you discuss with your co-directors the question of the utilisation of this £550,000?—I reported to them that it was the revenue of the year.

And as to its utilisation?—It arose.

So far as you remember, did you discuss the utilisation of the £550,000 in the year's accounts?—I mentioned the fact that we were getting this during the year. The Revenue paid it to us during that year, and it went in the normal course into the profit and loss account.

Do I understand you to say that in your view there was, or was not, an adjustment of taxation reserves that year?—It met the demands of the chartered accountants, and I saw no objection to it.

I suggest to you that if the shareholders had known what we now know with regard to the year 1926 they would have been disturbed?—Not if they had known it in 1926.

I think you said that they would have been gratified?—They would have been very pleased if they had heard in 1926 what the financial position of the whole group was—and very surprised.

Why did you not tell them in 1926? What was the need for keeping anything back?—There was no need to keep anything back.

Why was it desirable to keep anything back?—We published everything about the whole group.

So far as the shareholders in this company were concerned, would they have been disturbed by the result of the year's operations?—No.

Would they have been gratified?—I think they would have been glad.

Why, then, should they not be told about the result of the year's operations?—Because if you are going to do so, it is fair to them not to mislead them, and therefore, you ought to publish the whole details about the whole group in which they are intensely interested. It is not a very easy thing for the average man to understand; there were 35 companies in the group.

If it is not a very easy matter for the average man to understand, do you think that the ordinary man, looking at the accounts for the

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year 1926, would think that £150,000, and that alone, had been transferred from the reserves?—That is all that had been transferred from the reserves.

Do you think he would have realised that £550,000 was a special non-recurring item that had been brought in?—In a big group like this, you have constantly large non-recurring items coming in. That is my experience over the last twenty-five years, and you cannot judge this business by one year, or even two.

Would the shareholders have been disturbed if they had known that this item of £550,000, as a non-recurring special item, had been brought in?—I do not think the shareholders would have been disturbed, because the non-recurring amounts that came into the accounts of a big group like this were very large.

Why, in those circumstances, were the shareholders not told?—I did not consider that there was anything at all special to report.

Surely you must realise that it was a matter of great importance to the shareholders to know whether the accounts are swollen in any particular year by items of such a nature that they will not come in again?—If you know that there are other items in following years, I do not agree.

We know, to take an illustration, that the only other time that this thing occurred at all with regard to E.P.D. was in 1927, when the rest goes down. But surely you must distinguish, as a business man, between items which are normal earnings and items which are highly special and which do not recur?—I do not take the view, in regard to a great group of companies like this, that because a non-recurring receipt comes in in one year you must specify it; you have non-recurring receipts in many years.

Take a simple illustration. Is it important for a shareholder to know, in order to appreciate the true position, that the accounts of the year consist very largely of non-recurring items?—I do not think it is when he has confidence in and knows the class of men who are directors of the company, and the policy they have been carrying on for many years, which is one of sound, conservative—I use that word non-politically—finance.

Coming to the figures for the year 1927, they show that that year was better than 1926, and that the amount put aside for insurance that year was £211,000, substantially more than the amount for 1926, which was £162,000. The amount put aside for depreciation, however, was roughly £130,000 less in 1927 than in 1926?—Yes, but, of course, I am sorry to have to mention it, the depreciation is in every case far more than is necessary.

Then the deficit for the year 1927 is £334,000, as opposed to £540,000 in 1926?—It is better called a balance. I have told you from the beginning that I do not accept these as deficits.

I will use the neutral word "figure." The figure for investments in 1927 was £559,000, as compared with £267,000 in 1926, roughly £300,000 better. That was the result of the Nelson bonus?—Yes. It

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might have been a dividend just the same. It was actually a division of profits.

Will you agree with me to this extent, that a month before the Nelson Line bonus was declared, and a month after, the R.M.S.P. Company was exactly as well off?—I think that statement is grossly misleading. If by that you mean that the Nelson Line was one of the 100 per cent. companies, then there would be some substance in your remark, but then you must apply that to everything. The Nelson companies were two separate companies, and they were very successful companies.

Is it a fact that the R.M.S.P. Company was just as well off a month before as it was a month after this bonus was paid?—If any 100 per cent. company pays a £1 dividend to the parent company, the parent company is in exactly the same position financially as if it had not been paid.

Is not the significance of the figure this, that the £300,000 which the Nelson companies paid by way of bonus really represents, not merely earnings which the Nelson companies had made in the year 1927, but the earnings they had made over a series of years up to 1927?—Without having the Nelson companies' accounts before me, I should say "yes." I mean by my answer that the whole £300,000 profit was not made by the Nelson companies in that year.

In the 1927 accounts of the R.M.S.P. there are certain special credits, of a non-recurring nature, the extent of them being more than half a million pounds. Notwithstanding those facts, a 5 per cent. dividend was paid by the company for 1927, representing an increase over 1926, though £150,000 was taken from disclosed reserves in 1926?—In 1927 the company did not take anything from published reserves, which had been steadily increasing. The company had received £232,000 back in respect of income tax, and had received a profit of £108,000 on the sale of steamers, and £17,000 sundry credits.

I am pointing out that these special non-recurring items came to over £500,000. Under those circumstances, why did you move up the dividend from 4 per cent. in 1926 to 5 per cent. in 1927?—For this reason, that since 1925 the results of voyages had been steadily improving, except for the one break, which occurred at the time of the great strike. The curve was rising slowly, but it was rising.

Let us see what happened in those years. In the five years' period to 1925 you realised four millions of special non-recurring credits. In 1926 and 1927 you are using an extra million?—I think it fairer, in order that the whole position should be understood, to say this. The companies were in a very strong financial position.

I suggest to you that that is not true?—I know you do, and that is why I am trying to tell you the facts. I am talking of things I absolutely know.

You had a reserve fund of one and a half millions, and an insurance fund of £1,300,000, making £2,800,000; and in these seven years ending in 1927 you had utilised five millions of special non-recurring items—that is twice as much as your published reserve funds—to enable you



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to carry on?—You have mentioned five millions—I have not checked the figure—as if it were something enormous; but these companies had altogether over 13 millions of reserves, they had a fleet which cost over one hundred millions, which should have been written down to 60 millions, and was written down to about 54 millions. So that there was about 17 millions after all these had been paid, and you say: “What an awful thing; this company has actually used five millions to do something.”

I am not saying that this is an awful thing, but that at least it is a thing of which the shareholders should have been told?—I think the course taken by the court of directors was in the interest of the whole concern.

Do you think it would have upset the shareholders if they had known about the utilisation of that five millions over the seven years?—No.

Then again I ask, why not tell them?—I think we carried on the business in a way which was to the best interests of the company.

Do you think the shareholders would have been agreeable to your getting your commission in 1927, which amounted to £27,000, if they had realised the facts about that £5,000,000?—There was an occasion some years ago when I had thought that a commission of 1 per cent. was excessive, and I had it altered to  $\frac{1}{2}$  per cent. That alteration was carried unanimously at a general meeting of the company. It was not done by the board.

Now may I ask my question again? Do you think, if the shareholders had known that this £5,000,000 had been expended between 1921 and 1927, they might have raised some question as to the propriety of your getting your percentage on the takings in the year 1927?—I do not think they would have done so, although I might say that in 1928, when it was also due to me, I did not draw it.

Coming back to 1927, the special items amount to £512,000?—These are things that come in as the ordinary receipts of the company. There is nothing wrong about it; nothing that you have to apologise to anybody for, any more than a member of Parliament who draws £400 a year would apologise.

After all, people know that a member of Parliament is drawing £400 a year, and I am not suggesting that there would have been the smallest objection to any of these items in the accounts if the shareholders had known. What I am criticising is that you are utilising and putting to the credit of profit and loss account £512,000 in this year without the knowledge of the shareholders, thus enabling you to pay a dividend of 5 per cent., and, therefore, qualifying you for your commission?—The money comes in in the ordinary way; it is one of the receipts of the year.

Let me ask you about another receipt for that year—1927. There is a credit in respect of dividends and bonuses from allied or other companies of £559,000. Part of that was a dividend from the Pacific Steam Navigation Company amounting to £60,000. Is it the fact that that was paid as to £10,000 in cash and as to £50,000 by the transfer

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of ordinary shares in the White Star Line, 2s. paid?—I should not put it that way, but it was the net result. What actually happened was that the court of directors of the Pacific Steam Navigation Company offered to the court of directors of the R.M.S.P. Company these shares as part, and they took them.

So that the net result was that the R.M.S.P. received £10,000 in cash and £50,000 in shares, 2s. paid, so that the value of the shares was £500,000 with a liability in respect of uncalled capital amounting to £450,000?—I do not think it is quite accurately stated. The shares were not part of the dividend.

Did the holding of those shares involve the R.M.S.P. Company in the possibility of an enormous call for unpaid capital?—You have already explained to me that when a 100 per cent. company pays a dividend, the parent company is none the richer. Therefore, if the parent company buys unpaid shares from a 100 per cent. company, it must be none the poorer—or your argument must be wrong.

I think, if I may say so, that you had better not try a combination of logic and law?—I would not touch law for anything.

If the Pacific Steam Navigation Company, for instance, found itself confronted with a very large liability in respect of unpaid capital, and could not pay it, it could always be wound up?—Yes.

Were the shareholders of the R.M.S.P. told anything about these shares?—I cannot remember what I said then, but these things were published in the shipping papers directly a transfer was registered.

Did you sound any note of warning to the shareholders in 1927?—I do not think I said anything of that nature, but I cannot remember exactly all I have said in the last twenty years.

The directors' report for 1927 contains reference to the fact that the North American apple crop had not been so good as in previous years, so that the business of the company had been affected thereby. Did you not think that the shareholders would have been just as much interested in the transfer of £232,000 (received in respect of income tax) to the profit and loss account, had it been stated, as they were interested in the North American apple crop?—The statement about the apple crop was not made by me personally, but by the court of directors, and, indeed, it was a matter of very great interest to the company's business. I do not agree with your suggestion.

This report was published, and a 5 per cent. dividend was in due course paid, which was very well received by the press?—As I have already stated, the business was recovering from 1925 onwards.

A leading article was published in the *Financial Times* on 12th May, 1928, referring to the satisfactory recovery in the profits of the R.M.S.P. in 1927. The writer of that article was obviously under the impression that there had been no special non-recurring items brought into the accounts for the year 1927; and what I suggest is that when you made your speech to the shareholders, a fortnight after the publication of that article, you had a golden opportunity to correct any misapprehension?—You are suggesting that I read it at the time.

In your speech to the shareholders in May, 1928, you said that

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the accounts set out the position very clearly, and that the results for the year might be regarded as not unsatisfactory. Were those statements true?—They were.

Of course it was a very difficult time, and you were fighting very keen competition; in view of the difficulties of the time, you regarded the accounts of that year as not unsatisfactory?—In view of the difficulties of the time, I thought that the fact that the company was steadily doing better was very satisfactory, I think the expression I used was “not unsatisfactory.”

Do you really think the ordinary shareholder of the company would have had the slightest idea that in order to pay that 5 per cent. dividend you had to dip your hand into such matters as excess profits duty?—We did not dip our hands into it I object to the expression “dipping your hands.”

I did not mean to use an expression which might be misconstrued. If my words are clumsy, I am sorry. All I meant to convey was that this amount of £232,000 was brought in. Do you think that the ordinary shareholder would have had any idea that you were utilising that sum?—The sum which we had received during the year?

The sum which had become free during the year. Do you think the ordinary shareholder would have the slightest idea that you were relying upon such an amount as that?—I think it was quite a right amount to carry to profit and loss account.

That is not a proper answer to my question. Do you think the ordinary shareholder would have had the slightest idea that you were relying upon items such as that to pay a 5 per cent dividend?—I think it was a fair statement of the position.

I will try once more. (*Question repeated*)?—I do not think the ordinary shareholder would appreciate how such a great concern as this company was managed and must be managed.

At any rate, whatever the position would have been if the shareholder had been told things which he was not told, the shares remained steady. In fact, the ordinary shares went up, did they not?—I cannot tell you in the least. I have never been interested in the Stock Exchange prices of shares.

You do not follow the prices of your shares at all?—Very slightly.

I should have thought it was what a chairman of a company would do, because he would want to avoid violent fluctuations of the shares?—Oh, from that point of view, yes.

You agree that the ordinary shares might have gone up slightly?—Yes.

Do you think the position really justified that going up?—Yes, certainly. The business has been steadily improving since 1925—going up gradually.

Just look at Exhibit No. 13—or 19, I think, is the one for this particular year. It is a document which was produced at the court of directors. There is nothing here, is there, about an item of £232,000 being utilised?—No, that is not there.

If you discussed these things at the court of directors, why not

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have it down in black and white for the court of directors to see it?—The answer is quite clear, Mr. Attorney. The directors were passing a form of accounts in black and white, that was going to be published, with figures in red ink, giving the figures for the previous year. Each of the directors had this before him. I went through every item.

If these matters were discussed between you and the court of directors, how is it that there is no document ever put before the court of directors which showed these figures?—The directors get the amounts of every voyage put before them, and being all very intelligent men, they see what the debit and credit is, and how the totals compare with the previous year. They also see how the company's ships are doing compared with the corresponding voyages of the same year.

You may read through every voyage account, but you won't see this figure of £232,788, will you?—No.

Why is there no paper before the directors which shows that is going to come into the account?—It does come into the account, and they all know it.

I have got this controversy between you and Mr. Cason. If it is a fact that these things were discussed at meetings of the board, I should have expected to find some piece of paper on which these figures were written down, so that they might be before your own board, and I do not find it?—I would have the particulars before me. The whole question of how the company was doing was being constantly discussed. Our board meetings take from one to one and a half hours. We discuss how the company is doing, and we then lunch together in a private luncheon hall, where things are again discussed. I constantly see my colleagues in between courts, and the majority of them know as much of how the company is going on as I do myself.

Is it a fact that there never was any paper put before your fellow-directors showing, for instance, how this £232,000 in connection with excess profits duty had been brought into the account for the year 1927?—I could not say yes or no to that. I could not say exactly what was done four years after. I have not got the happy legal memory that members of the Bar have.

Do you really tell me that if, with regard to those accounts for the year 1927, instead of making the speech you did, you had told the shareholders exactly what the history of this company had been for the last seven years, that the price of those shares would not have fallen down straight away to practically nothing?—I cannot express an opinion on that; you might as well ask me if in some of the years when we earned 15 per cent., but only paid 6 per cent., we had paid out 15 per cent. the shares would have gone up in price three times over.

Would there have been a panic if you had told your shareholders what we now know?—I do not think there would have been any panic. It would not have been in the interests of the company, and it would have enormously encouraged competitors.

You mean this, that if your competitors had known how desperately difficult the position was becoming, they would have been cheered up?—

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Not desperately difficult. I don't agree with your language at all. I entirely disagree with your language

Let me put it this way, then. If your competitors had known how difficult the position was becoming, they would have been cheered up?—I could not even agree with that. If they thought we had been doing a little worse, it might have encouraged them. I do not use any of that strong language.

If one assumed that the company was flourishing, building up huge reserves, and so forth, would the publication of that information encourage competitors?—I think it would. You could encourage competitors by showing them that you were doing magnificently.

Do you encourage competitors by telling them that you have not made a profit since 1920?—I do not agree with that statement. It is absolutely untrue.

Do you encourage competitors if you tell them that you have not had enough out of current earnings, after providing for depreciation, to pay debenture interest?—That is not true

In which year, since 1920, do you think there was enough out of current earnings, after providing for depreciation, to pay debenture interest?—I think your statement is incorrect

In which of these years do you think there was enough to pay debenture interest?—I think, Mr. Attorney, that is a very misleading question.

Which year is the year in reference to which that is misleading?—I think it applies to several of them

Tell me one of them?—I would rather put it the other way. In the year 1926 there was not sufficient to pay debenture interest

Is your answer then that there was enough in every other year out of current earnings after depreciation?—No, I didn't say after depreciation.

What I am putting to you is that in no single year since 1920 had you been able, after depreciation, to pay your debenture interest out of current earnings?—I entirely disagree.

We will leave it at that. With regard to the year 1928, is this right, that in 1928 the words "Adjustment of taxation reserves" had disappeared?—Yes.

And instead of them I find "after crediting income tax reserves not required"?—Yes.

Do you agree that according to the table which is before the Court, the item referred to accounted for a sum of £350,000 brought into the accounts for the year?—Yes.

If you publish that to a shareholder, the shareholder knows that the balance for the year has been swollen by the crediting of income tax reserves not required?—Yes.

Why did you change your language?—I do not know how that originated. It might have been done by the accountants' staff, but I do not know.

You appreciate the difference between the two, do you not?—Yes, absolutely.

# The Royal Mail Case.

Lord Kyleant

I have now to come to another part of the case. Let me ask you from the point of view of the prospectus a few questions. Do you think that the duty of a person who puts forward a prospectus is to put forward all relevant facts, fairly and squarely, so as to enable an investor to form his own judgment?—Yes.

And you would agree, would you not, that it would be deplorable if that standard is ever departed from?—I agree.

And deeply deplorable if that standard is departed from by a man in a high and eminent position in the City of London?—I agree.

Did you put forward all the relevant facts in your possession to enable the investor to form his own judgment?—I put forward absolutely a true and correct statement, and I took those steps. Not only was it first passed by one of the leading firms of solicitors in the City of London, but then, at my request, they submitted it to a leading counsel. I said: "Who is the best man to consult on this particular question and work?" They mentioned the name of a distinguished member of the Bar, and we got his opinion. Then before that, or after that, it was twice before my colleagues and was very fully discussed, and in my view it was an absolutely straight, true, and fair description of the company.

Do you state to the jury that you put before the investor all relevant facts, so that the investor might have all material on which to make up his own mind—did you?—I say yes.

In fact the issue was very largely oversubscribed?—Yes.

And, of course, the issue was not in the nature of a gambling thing. It would have been regarded, would it not, as almost in the nature of a gilt-edged security?—At that time the security over and above the debentures issued was over £14,000,000, and even to-day it is many millions.

You see the paragraph beginning "Although this company." It goes like this: "Although this company, in common with other shipping companies, has suffered from the depression in the shipping industry, the audited accounts of the company show that during the past ten years the average annual balance available, including profits of the insurance fund, after providing for depreciation and interest on existing debenture stocks, has been sufficient to pay the interest on the present issue more than five times over." Do you remember the history of those last few words which appear in leaded type? Why were they put in in leaded type? Was it because it was a very important factor in enabling the ordinary investor to make up his mind?—It enables anybody who doesn't want to read the whole prospectus to see what was the position, and whether it was worth going into further.

And was it any criterion of the future prospects of the issue?—I was not responsible for them being put in with any idea of prophesying what the future was going to be.

Did you intend the investor to be guided by this consideration, "This is what the company has done in the past and presumably will do in the future"?—It is telling him what the company has done in the past and what it may do in the future.

## Evidence for Defence.

Lord Kylsant

Exactly. It is simply given in so far as the past may give some indication as to the future?—Yes.

Is it a fair indication as to the present earning capacity of the company?—In my opinion it was at that date an absolutely fair and accurate statement of the position, bearing in mind that the business had been steadily improving since 1925. It was a little better in 1926 and still better in 1927.

Do you remember telling me this morning that the years 1918, 1919, and 1920 were abnormal years?—Yes

How can it be fair to ask the investor in the year 1928 to judge the future by the past if you take a period of ten years which has three absolutely abnormal years at the beginning of it, and obscures altogether the difficulties of the period as a whole?—I do not think there is anything misleading about that. Everybody knew about the Vestey competition. It was no secret, and it was known over the whole of Great Britain.

This is the critical question, is it not: Supposing, instead of setting out average annual balances, you had set out the balances year by year, corrected as they would have been if Mr. Morland had written back those items into the appropriate years, you would have seen, would you not, that the great bulk of the money was earned in the first three years, which were followed by seven very lean years?—Less prosperous years.

A letter has been produced, in which reference was made to writing back certain items into what were suggested to be appropriate years. The result of that, if it had been done, would, I suggest, have been to show profits in the early years and deficits later on?—That would have been very misleading. I think you are entirely mistaken about that.

Would it have shown that the first three years were very much more profitable than the others?—Oh, yes; that applied to practically every business in Great Britain.

Then what is the relevance of asking the shareholder to make up his mind on figures based on an abnormality which occurred some ten years ago?—We are living in an after-the-war period, and you have to set out the thing in the fairest way possible. The court of directors gave the result of the dividends paid in the years.

What relevance have the years 1918, 1919, and 1920 as a means of judging the earning capacity of 1928?—Shipping went up and down, and there were cycles exactly like the waves of the sea. The year 1920 was the top of the wave.

Was not the abnormality of 1918, 1919, and 1920 due to the war?—The abnormality of 1914, 1915, 1916, 1917, and 1918 was entirely due to the war—naturally. We passed our dividend in 1914, and we showed that we had passed it.

About 1919, was not that abnormality a consequence of the war?—That was the beginning of a rise, and 1920 was the crest of a wave.

In 1920 the abnormality was in part due to the war. Does that represent your view?—No. In the year 1918 the abnormality was

# The Royal Mail Case.

Lord Kylsant

entirely due to the war. In 1919 a little part was due to the effect of the war, but 1919 and 1920 are really the ordinary crest of the wave.

If that is true, why did you tell me this morning that those years were abnormal?—So they were, because the war had a certain effect upon them. It is awfully difficult to explain in cross-examination.

Will you explain to me why you thought it possible that any intelligent investor ought to have based his calculations for the year 1928 upon the earnings of the company in the years 1918, 1919, and 1920?—I think it was right to give them that, although they knew that those three years would be rather more than normal crests.

Supposing you had set out those years, year by year, showing great profits for 1918, 1919, and 1920, and then the figures being written back as Mr. Morland was going to do, showing the figures for 1923, 1924, 1925, 1926, and 1927, do you think there is a single person who would have invested in this debenture stock at 92½?—Of course, I cannot tell what Mr. Morland's figures would have been. I think the majority of people invest in a thing like this when they know that there are fourteen millions between them and foreclosure.

If you had set out these figures year by year, do you think that people would have invested in the shares?—Yes. When the figures were set out accurately, not as you have been setting them out.

As Mr. Cason has been setting them out on this sheet. If they had been set out as they are set out on this sheet, no investor would have invested his money?—No, because that is absolutely inaccurate. I never saw that statement before I came into this box, but in my view it is grossly inaccurate.

If the facts had been set out in the prospectus, as they have been set out in Exhibit No. 21, do you think anybody would subscribe to this issue?—If they had been set out as they have been proved to be in this Court, there would have been a good response to this issue.

With regard to what I have called "the depletion of unpublished reserves," would it be an honest statement to say in the year 1923, "I have added to the reserves," when what you have done is to add to your published insurance reserve and drawn more than £80,000 from your unpublished reserves?—I don't admit we have drawn anything from the reserves, and that is fundamental.

You say that all the way through?—I say that all the way through, except in that one £50,000.

Is it your view that if you had withdrawn anything you ought to have disclosed it?—I have not gone so far as that.

How far would you go?—In certain cases, so long as there were very large sums of published reserves, I should not think it necessary to publish anything. That is my personal view.

You were going to raise £1,850,000, paying brokerage of £1 per cent., so the net figure would be rather less. May I take it that more than half the money was already required to pay off the existing bank overdraft?—We had just built one of the finest buildings in the City of London. The land itself was worth half a million, and £750,000



## Evidence for Defence.

Lord Kyleant

was spent in the building. That was the reason why there were overdrafts; builders do not put up a building in a year.

Sixteen months after you made this issue, are you applying to the Treasury for an extension of the guarantee?—Yes. Only in the case of £5,000,000 which my late friend, Lord Pirrie, arranged with the Treasury, and for five years. I told him at the time I thought it would be dangerous to take five years, and he said: "There will be no difficulty in getting it extended to ten or fifteen years." Unfortunately, he died before it fell due. That is the story about that.

A relevant circumstance to bear in mind when you decide what dividends to pay?—Yes, but I had information. I was in direct touch with the leader of your profession, and he told me not to be worried about it; the cards were in my hands.

Anyhow, you hadn't this card in your hand—the ability to pay what you owe?—As the Treasury did not extend the guarantee, there was a difficulty, and that is the reason. But the debenture-holders of this company are well protected still.

Are they?—Yes

What is the price?—I cannot tell you what is the price.

What is the price to-day?—I don't know.

Do you mean to say you don't know?—I do.

Do you tell the jury on your oath that you cannot answer that question?—I can give no other answer except that in my view the debentures were fully secured.

It is to me a most extraordinary thing that you should tell the jury on your oath that you haven't the least idea —?—I didn't say I hadn't the least idea.

What is your idea, then?—I haven't looked at the matter for some days.

But, when you did last look, what do you say about that?—They did go down very low at one time. But they have since gone up, nearly double, I think.

By Mr. Justice Wright—Will you tell me what is the date of the guarantee?—It would be about nine years ago.

By the Attorney-General—I thought you said five years before?—I think I said about seven years.

By Mr. Justice Wright—And for what period was it?—For five years. And the associated companies raised just over £12,000,000, and they have paid over £2,000,000 in reduction, and they have paid every penny of interest up to date. The Government did not see their way to agree with the suggestion made two years before to continue it for five years.

*Cross-examination continued*—In addition to other matters, were you not under an obligation to find no less than two and a half million in connection with your White Star commitments?—Yes. The total money raised was just over £12,000,000. We paid the instalments due, which were £2,000,000, and there were just over £10,000,000 still running, but it was this £5,000,000 which caused the trouble, because the guarantee was only five years.

# The Royal Mail Case.

Lord Kylsant

Now let me summarise the case I put to you here. I don't ask your assent to it, but to the fact that this is the way it is put against you. From the year 1921 to the year 1927 inclusive your company has steadily been making losses and living on items which came in in respect of its previous years?—I don't accept your statement of the position.

But you expended £5,000,000 in reference to recurring items of expenditure?—It may be so.

And that these all owed their origin to these years?—No, I don't agree with that.

And that if you had set out these facts, there was no chance of anybody investing a penny piece in this issue?—I absolutely disagree with your facts.

That to avoid setting out these facts you took the average for ten years, mixing up the whole abnormal period—that new period in which new conditions prevailed—and that that was done deliberately—

Lord KYLSANT (*emphatically*)—No

Dishonestly?—No.

And with the intention of defrauding those people who might be induced to invest their money?—No, absolutely untrue

Re-examined by Sir JOHN SIMON—The Attorney-General has been asking you whether you think that anybody who knew year by year the course of the company's affairs from 1918 to 1927 would have subscribed for this issue. You knew the history of the company for the past ten years. Did you subscribe to the issue?—I very seldom buy debentures. I confine myself principally to ordinary shares.

I am asking whether you subscribed?—One of my private companies did.

It was your money?—Yes

Were there trust companies under your control that subscribed to this issue?—I know they sent in applications.

As a matter of fact the full application was over-subscribed?—Very largely.

I want the jury to understand this. Is it a fact that you, yourself, believed that this was an issue properly to be subscribed?—Yes.

The Attorney-General has asked you a good many questions about the "average annual balance," and has called your attention to the fact that at the beginning of this period of ten years the figures would be better, and that later they would reflect the depression in the shipping trade. Will you look at the paragraph? Do you observe that it begins with these words: "Although this company, in common with other shipping companies, has suffered from the depression in the shipping business"?—Yes.

As you understood the matter, you were stating an average of ten years, indicating that at the end of the period the figures are worse. Do you regard that as an indication to those who read the document that the position would be better at the beginning and worse at the end?—That was the meaning of that.

You were asked why you chose ten years. It is not uncommon,

## Evidence for Defence.

Lord Kylsant

when issuing a prospectus, to state an average for a considerable number of years back?—I think it is a very ordinary thing.

This prospectus, I imagine, was authorised by the other distinguished members of your board?—Yes; we had meetings specially to discuss it.

In your experience of them are any of them capable of authorising a statement that they knew to be untrue?—I should say absolutely no.

Now let us look at the ten years period a little more closely. It begins, as the Attorney-General has pointed out, with three good years?—Yes.

In so far as the years affected by the late war were concerned, the facts were as well known to the man in the street as to you?—Yes

In May, 1927, was it your view that the trade of the country would recover?—Yes. Indeed, I saw aspects that were distinctly encouraging, and I indicated at that meeting my belief in a favourable turn of events. That was in my considered judgment the position at that time

In your view of the cycle of trade, was it your belief that it had touched bottom and was beginning to rise?—That was my honest belief.

You said: "I am a believer in the principle of trade cycles, and throughout my business life have seen that it has been of seven to ten years' duration." And this is before the prosecution?—Yes.

You incline to the view that an upward movement had already begun?—Yes.

You have heard the suggestion in cross-examination that the accounts published were calculated to lead shareholders to think that you had had a good year from the point of view of profit and loss. Would you mind looking to see who it was who moved the vote of thanks to you?—Sir John Fortescue Flannery, M.P.

And I see that in moving it he says this: "That the company was eighty-eight years old, but there were no signs of senility, but, on the contrary, there were signs of activity, vigour, and enterprise, and it was true that they had not had a good year from the view of profit and loss." Were you there when he said that?—I was there.

That doesn't look, does it, as though your published report and balance sheet had misled the shareholders into thinking that it had been a good year?—I quite agree.

That is the year 1926. Now take 1927. Is it quite clear now on the figures that 1927 was a better year than 1926?—Certainly.

Did you take that as a further indication that the wave was still on the rise?—I did.

Is it not the general experience of any one who understands a business, that once you get this cycle of seven, eight, or nine years going through a depression, when once the rise begins, is it, in your experience, continual?—In my practical experience it always is.

Passing on to twelve months later, to 1928, did you hold the view that the improvement was going on?—I did, very firmly.

The North American apple crop for that year was considerably below the normal, and therefore shipping was smaller than in 1926.

# The Royal Mail Case.

Lord Kylsant

It looks as though you had mentioned this in your speech as a warning that a very important source of trading had got worse?—Yes, one of the sources.

Then, until this economic blizzard that followed, and then the initiation of this prosecution, has it ever been suggested to you that the profits for the ten years we have examined were not a fair average?—Never.

We all appreciate the wide experience you have had of shipping concerns; is this ebb and flow as between 1918 and 1927 characteristic of the general course of British shipping?—That is so, and books have been published on the whole question of shipping cycles.

As you understand the matter, do you see any objection to the bringing in of any of the figures that appear in the balance sheet?—No.

The suggestion is that something special should have been said about it. Do I understand rightly that these items which appear as special credits are one and all of them of the nature of receipts and distributable receipts?—Yes

No doubt some of them have a history behind them, but so far as you know they are distributable receipts?—Distributable.

In 1926 £270,000 cash was received by the company from the Revenue?—Yes.

In your view, is that a receipt of the company in the year?—Certainly.

In addition to that, in that year, was another £551,000 received from the Government in the year by way of constructive repayment?—Yes.

And the accounts for 1926 are not settled or drawn up until the spring of 1927?—That is so.

By that time, the situation was still more cleared up?—Yes.

As you understood the matter, and understand it now, do you know any reason why these sums should not be regarded as distributable receipts in the year?—I know of no reason.

Is that how you did regard them?—Yes, and we acted accordingly.

In July, 1926, £70,000 was paid by the Revenue to the company in respect of relief under a section of the Income Tax Act?—Yes.

As you understood the matter, is that received in the year?—Yes.

It is in the nature of a proper distributable dividend item?—Yes.

Do you know any reason why you should address the shareholders and tell them you had received that £70,000?—I know of no reason.

On the other hand, there is one definite transfer from a published earmarked fund?—Yes, £150,000.

When you look at the profit and loss account, do you notice that the word "reserve" comes twice?—Yes.

So far as you understood the matter, did you regard that as an indication that the adjustment of taxation reserve was quite separate from the transfer from the published reserve?—Yes

You are aware that the adjustment of taxation reserve in 1927 consists of two items, one income tax of £120,000 and the other E.P.D. figure £232,788?—Yes.

## Evidence for Defence.

Lord Kylsant

Evidence has been given for the prosecution that the E.P.D. figure could not have been distributed sooner?—Yes. It seems natural to me that it should go into the ordinary receipts of the year.

It has been suggested that the special credits should be specially mentioned. Has anybody ever reproached you because you did not mention the special debits to the shareholders?—No

You, in fact, never did?—That I know.

And whenever, having earned distributable profits, you put any portion for the time being aside, you make no statement to the shareholders, and no one complains?—That is so.

Have you done anything more than bring the sums back and distribute them later on?—No.

Do you know of any reason why a man should be prosecuted for not having stated when you bring it back, although it is quite right not to mention it when you take it out?—I absolutely fail to follow the line of argument of the Government.

BRIAN O'DONOGHUE MANNING, examined by Mr. SINGLETON—I am a Fellow of the Institute of Chartered Accountants, and a partner of the firm of Messrs. Cole, Bond & Co. I assisted in the preparation of Exhibit No. 105, which has been used in the course of the case. That document in one column sets out the rate of dividend which was paid in each of the years from 1911 to 1927. It also shows the actual dividend that could have been paid in the various years, and the figures are correct so far as could be ascertained from the books of the company. After the year 1914, when £200,000 was taken from the reserve fund, there are six years in which there was put to reserve from profit and loss £1,360,000 in all. That was money which, if it had not been put to reserve, would have been available for dividend purposes. In the result the reserve fund in 1927 is greater by £1,180,000 than it was at the commencement of the period. Apart from that, there was some figure in the reserve fund before; in 1911 it was £80,000. With regard to the insurance fund, in every year since 1911, apart from 1914, there was an addition to the insurance fund. It is a free reserve. In column 5 of that document I set out the total increase in reserve between 1911 and 1927, which gives the figure £2,231,785. That figure, so far as I can trace, is correct. I then show the dividends that could have been paid. The dividends which were paid in the last few years were paid without drawing on these published reserves, except for the £150,000. I heard Lord Kylsant describe Exhibit No. 21 as misleading. With regard to the place where "deficit" appears in that document, in my view, in arriving at the results year by year in connection with that company "deficit" in that part of the page does not express the true position.

The Court adjourned.

# The Royal Mail Case.

Seventh Day—Tuesday, 28th July, 1931.

## Evidence for the Defence—continued.

BRIAN O'DONOGHUE MANNING, further examined by Mr. SINGLETON—With reference to Exhibit No. 21, and taking the year 1921, there are three items at the bottom of the column which are described as special credits. Those are all items which were received during the year. In my view they are properly distributable as profits for the year. In the next year, 1922, there appears among special credits E.P.D. £100,000. The position with regard to E.P.D. then was that the company had made provision in its books for the expected liability for E.P.D. over the seven-year period. It was ascertained in 1922, although not definitely, that that provision was excessive, and it was decided to take £100,000 as the liability had been over-provided for. That, in my view, is not properly described as a reserve. It is not a reserve; it is a provision for liability. The provision for E.P.D. was a provision for a liability which proved to be excessive, and therefore any surplus was regarded as a profit for the year and distributable as profits for the year. It is not right to describe either the £550,000 which appears as special credit in 1926, or any items for 1923 appearing as special credits, as being transferred from reserve. I have before me Exhibit No. 94. Dealing with the year 1926, that document shows an item of £236,000 odd as at 1st January, 1926. There is tax deducted from dividend, £121,237. That is a figure which the Attorney-General agrees is something received in the year. There was taken among special credits £175,000, the figure which is given on Exhibit No. 21. The figure £121,237 is a figure which the company gets or acquires in the year 1926. The figure of £70,000 is a section 34 claim. That is a claim arising under section 34 of the Income Tax Act, which can be made in any year when the company has made an adjusted loss. If the claim is made and allowed, there should be a definite increase in the amount which is distributable.

By the Court—The £121,000 arises in respect of the dividends paid or deducted during the year, and the £70,000 is in respect of an overpayment in the previous year. They are both matters which may fairly be credited during the year?—Yes, my lord.

*Examination continued*—With reference to the 1927 account of the company, I heard yesterday a suggestion that the Pacific Steam Navigation Company in 1927 had paid their dividends by £10,000 in cash and half a million White Star shares. That transaction does not come at all into the 1927 accounts of the Royal Mail Company. The dividend which was declared by the Pacific was credited in the books of the Royal Mail on 13th June, 1928.

Examined by Sir PATRICK HASTINGS—Did you hear some questions put to Lord Plender?—Yes.

## Evidence for Defence.

Mr Manning

In your view, are the words which are used in this case, "adjustment of taxation reserve," usual words used by accountants?—Yes.

And, having regard to the facts as they have been elicited in this case, in your view were they appropriate words for Mr. Morland to have used in 1926 and 1927?—In my opinion they were.

Supposing you had been the auditor of the Royal Mail Steam Packet Company in 1926 and 1927, would you have signed those accounts as Mr. Morland did?

Mr. JUSTICE WRIGHT—Before the witness answers that question, do you object, Mr. Pritt?

Mr. PRITT—I would rather not.

Sir Patrick Hastings then put the question again, and witness replied, "I should."

Cross-examined by Mr. PRITT—The chairman of a company sometimes looks at the accounts from a different point of view to the accountant.

With regard to this Exhibit No. 21, you will remember that Lord Kylsant has described it as grossly misleading, and you have described it as misleading?—Yes.

Is this a document prepared by the chief accountant of the R.M.S.P.?—I understand that this was a document which the chief accountant kept himself for memorandum purposes.

Mr. JUSTICE WRIGHT—I don't remember Mr. Cason being challenged as to the accuracy of the document.

Mr. PRITT—It was never suggested to him that it was misleading at all.

*Cross-examination continued*—With regard to the document you have assisted to prepare showing that if the R.M.S.P. in the years prior to 1926 and 1927 had been minded to declare larger dividends it could have done so, that is a book-keeping position?—Yes.

Before a company declares a dividend, it considers its book-keeping position, but also its cash position?—Yes

Have you examined the cash position at the time?—No.

It would, in fact, be a very difficult task now?—It would involve a very detailed examination.

You are unable to say that the company's cash position would have enabled them to pay these dividends?—It does not mean that there must be a cash balance when a dividend is declared.

By the Court—Whatever your assets were, you might be brought down simply for want of cash?—Yes. It frequently happens that when a large profit has been made there is no cash to pay the dividend

*Cross-examination continued*—Dealing with the E.P.D., you told counsel that you did not regard, in the circumstances of this case, the various sums laid aside as a reserve, but as a provision for a liability?—That is so.

Do you know many accountants do call it a reserve?—Yes.

You would never say that any of your professional colleagues were wrong when they do so describe it?—The facts are the real thing.

By the Court—I understood that the company actually paid over

# The Royal Mail Case.

Mr Manning

to the Treasury about £1,200,000 in direct taxation and got back about £1,000,000. Part of the amount was dealt with by constructive repayments, and therefore did not come into any cash account. The proper liability for E.P.D., as it turned out, was about £1,700,000, but they knocked off £1,400,000 for obsolescence and deferred repairs, so that all the Treasury eventually got was about £340,000?—Yes, which included the obsolescence allowance.

The obsolescence allowance really arises as an allowance from the E.P.D.?—Yes. That was the convenient way of making the allowance. It was intended that an allowance should be made, and it was more convenient that something should be allowed from what had been paid or assessed than that it should be a new form of grant.

Re-examined by Sir JOHN SIMON—I understood you to say that there was a distinction between the way in which income from subsidiaries was taken and the way in which the matter was regarded when it came to pay dividends out. Supposing the R.M.S.P. only had one subsidiary, which declared a dividend requiring £100. After deducting income tax, the amount handed over by the subsidiary would only be £80?—Yes.

Could the R.M.S.P. distribute to its shareholders the gross sum of £100, which the subsidiary had declared as a dividend?—Yes.

Because, when it declared a dividend of £100, there would be a special credit of £20?—Yes.

By the COURT—You could distribute £100 nominally, but pay £80 and credit the company with £20?—That is so.

*Re-examination continued*—Regarding the provision for E.P.D. made by the company between 1915 and 1921, the total provision was £2,260,000, but it turned out in the end that there was an over-provision, and the final liability was £1,700,000?—Yes.

Let us suppose a company that never made any excess profits at all. Would it still, if it was a shipping company, have been entitled to obsolescence allowance?—I imagine it would.

Mr. JUSTICE WRIGHT—Does the witness know?

*Re-examination continued*—The payment by the Government of obsolescence allowance to a company would not depend upon whether they were making excess profits or not. The obsolescence payments do not arise out of any payments made by a shipping company to the Government, but come under an independent head. The obsolescence allowance came to £1,190,000, and the deferred repairs allowance to £238,000, or a total of £1,428,000. In 1927 the final payment was made by the Government, the whole thing was settled, and £232,000 was brought to the profit and loss account?—That is a correct statement of the position.

In your experience, do accountants in practice, in making or approving profit and loss accounts for the year, distinguish between what have been called non-recurring items and recurring items?—No.

When you are dealing with an enterprise of this sort, with all the subsidiaries and ramifications, do what are called exceptional items occur seldom or frequently?—They occur frequently.



## Evidence for Defence.

Mr Manning

In your opinion, after investigating the accounts very closely, is there anything misleading in not labelling non-recurring items and not disclosing them?—No.

At the first hearing, the Attorney-General, speaking of the year 1926, said: "You only get that balance by bringing into the year £750,000, which in no way ought to appear here at all" As an accountant, do you regard the £750,000 as money which ought not to appear in 1926?—No.

All these special items are undistributed profits?—Yes.

Until they are distributed?—Yes.

### Opening Speech for the Accused H. J. Morland.

Sir PATRICK HASTINGS—Members of the jury, you heard a sentence from Sir John Simon which I am going to borrow. He said that it was very bad advocacy to put one's case too high, and I agree with him; but there are no heights which I can put my case on behalf of Mr. Morland which are too high. I have only asked about a half-dozen questions in the whole of this case. You may not have seen the relevance of them, but they were vital. They led to answers which I knew must be given, and answers which once and for all put Mr. Morland back into the position in the eyes of all who read them that he enjoyed before May of this year. I am not concerned with exhibits in this case. I am not concerned with the examination of any document except the one in respect of which I am charged. I am going to ask you just for a few moments to consider with me the position of the gentleman who is now sitting in that dock, a place intended for thieves, cheats, people who rob their fellows, trick them out of their money or their goods. I am going to ask you to consider whether Mr. Morland is a man who is properly in that dock. I just want to tell you who he is. Until May of this year Mr. Harold John Morland occupied a position in the world of which any man might have been proud. He had lived a long life, a very useful life; there was not a man in the City of London who occupied a higher or a more respected position than he did. He was a member of a firm of accountants, Messrs. Price, Waterhouse & Co., a firm I suppose whose name and reputation are known wherever the English language is spoken. Mr. Morland was a partner, an honoured partner, and a respected partner in that firm, and was honoured and respected by every professional man in the City who knew him. For many years he had been the nominal auditor of the Royal Mail Steam Packet Company—and I use the word "nominal" for this reason, that you appreciate by this time that it was Messrs. Price, Waterhouse & Co. whose servants and clerks audited these books. It was the habit, and, I think, the requirement of the Royal Mail Company, that an individual should appear as auditor, but the clerks were not the clerks of Mr. Morland, they were the clerks of Messrs.

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Price, Waterhouse & Co. Mr. Morland for years audited this series of accounts. The Royal Mail meant no more to them than hundreds and thousands of big companies, banks and others, all of whom are audited in exactly the same way by exactly the same firm. Some question was raised about remuneration. The firm received a fee of 400 guineas a year. If it interests you to know, I asked Mr. Morland what in money as a partner the audit of the books of the Royal Mail meant to him. It was something in the neighbourhood of £20 a year; that was all.

You will ask yourselves, no doubt, did Mr. Morland ever own a share in the Royal Mail, did he ever buy a share, or did he ever sell a share? Did it matter to him personally whether they made millions in the year or anything? It mattered not at all. His only sole object, his only sole interest in this case in the last twenty years has been to do his duty as an auditor. And what was it? In a sentence I am going to tell you what it was. Every year the accounts of the Royal Mail were prepared by the accountant's department of the Royal Mail. Their accuracy of figures was checked by the clerks from Messrs Price, Waterhouse & Co., and then, when they were finished and everything was done, they went to the Board of the Royal Mail Company.

We are not living even to-day in this Court in the world of Alice in Wonderland. I decline even to consider the proposition that the Board of the Royal Mail did not know what was the financial position of this company year by year. Look at the names of the members of the board. Among them is the name of a man who, if things had been a little different, might have been standing here in this row where we are, one of the greatest commercial lawyers practising in London to-day. Is anybody going to tell me in this Court that Mr. Morland must have thought that Sir Leslie Scott did not know month by month and year by year the exact financial position of this company, when the very accounts prepared by the Royal Mail were sent up to the office where he and the board were sitting, were examined, and never came before Mr. Morland in his life until they had been passed by the board?

It is suggested in this case, in the wording of the indictment, that Mr. Morland in some way aided and abetted Lord Kylsant to do something. You will hear that never once in all these years did Mr. Morland ever speak to Lord Kylsant about the accounts. He was no more guided by his view than he would have been by the views of the office boy. These accounts, as he believed and knew, were the accounts of the directors of the Royal Mail, and they were sent to him. All I tell you about the accounts, as far as Mr. Morland is concerned, is this, that ever since 1921 he thought that the directors of the Royal Mail were acting properly; they were putting into the right and proper year amounts which they could rightly and properly utilise to pay their dividends. Year by year his duty was to take in his hand this printed document, to see whether the balances were right, whether the assets were right, whether the liabilities were right, whether the sums transferred in the year were sums which could properly have been transferred,

## Opening Speech for Mr. Morland.

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and sums out of which dividends could properly be paid. That went on until the year 1925. In 1925 Mr Morland did a thing which apparently to most auditors was even in excess of the strict requirements of his duty. He came to the view that a time had arrived when he ought to give to the company and its shareholders an indication that these amounts were being drawn upon or utilised for the purpose of paying their dividend. He never consulted with a soul. He never asked Lord Kysant to choose a form of words. The words that were used, "Adjustment of taxation reserves," are words that I might almost say are hallowed by usage. You may remember that I did not put to Lord Plender when he was in the box, bundles of profit and loss accounts audited practically by every firm of accountants, and if it were necessary to look at them one would find in every one of them the expression, sometimes in slightly different form, "Adjustment of taxation reserves." You will remember when Lord Plender went into the witness-box I asked him a simple question: "Is the expression 'Adjustment of taxation reserves' an expression commonly used by auditors?" His answer was "Yes." I asked him: "What is it used for by accountants?" and he said: "It is used to indicate that there have been transfers from reserves." "Reserves" is the word commonly used by accountants to indicate the very thing that happened in this case. The next question I asked him was this: "Does that word apply to cases where the transfers or allocations are small or if they are large?" Lord Plender's answer was: "They may be either large or they may be small." Then I said to Lord Plender: "What would you understand by the expression 'Adjustment of taxation reserves'?" He said: "I should understand that in order to arrive at this figure there were transfers from reserves, which might be large or might be small, but it gave to the shareholders every opportunity, if they desired to know, and if they thought they no longer trusted their board, so that they could have insisted upon knowing, of asking for themselves." Those are the very words Mr. Morland chose, without any suggestion, or without any conference with Lord Kysant, or any of the directors. He took upon himself the responsibility of taking accounts which had been passed by, amongst other people, a gentleman who was implicitly trusted by every member of the Bar. Mr. Morland himself said he wanted these additional words put in. He thought it right that they should go in, and they went in. That is why he is in the dock. There is nothing else at all. That is the only charge against Mr. Morland.

In 1927 there came a time when Lord Plender was asked to inquire into the affairs of this company for a purpose quite unconnected with anything we are here considering. It is a matter which I personally shall never cease to regret. Lord Plender himself no doubt had other business cares and was unable to investigate these matters himself, and another gentleman was asked to make these inquiries, which he did. Members of the jury, there are great men in all professions. Those of us who sit here may sometimes have to inquire into the affairs of one of our brethren, and, unless there is any reason for secrecy which

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makes it impossible, I should be sorry indeed to think that any one of us in such an inquiry, if we thought there was anything which required an explanation, did not go to him and say: "What is the explanation?" Of course, on the other hand, if there was nothing which required an explanation, it would not be necessary to go. One of two things has happened in this case, and I hope you will be as charitable as I am. Either Sir William M'Lintock, in looking into these accounts, seeing these balance sheets and making his report, saw nothing which even required an explanation from Mr. Morland, in which case it is only right and proper that he should ask him nothing. I cannot believe that there is another alternative; we have not heard it. I cannot believe that Sir William M'Lintock ever thought that Mr. Morland had committed even a slight error. He did not say so. If he did think so, and if he did not ask Mr. Morland's explanation, he must have had many sleepless nights since the day this summons was issued. On 13th May a criminal summons was served upon Mr. Morland to attend the Guildhall to answer a crime, a charge under the Larceny Act. On behalf of Mr. Morland a letter was written to the Director of Public Prosecutions saying: "We know nothing about this case. Can it be something which has appeared in the report of Sir William M'Lintock? May we see it?" and the Director or some one in his department said "No, you must wait till the case is opened against you by the Crown." What else could Mr. Morland do? In Mr. Morland's profession a man can go either to the president of the Institute of Chartered Accountants or the president of the Incorporated Society of Accountants. Mr. Morland went to both; he went to Mr. Hill, and he went to Mr. Morgan. I may say at once that I could not pay a high enough tribute to Mr. Morgan for the hours of time that he has taken in trying his best to see the rights and wrongs of this case. Into that box will go both of these gentlemen, the heads of their profession, coming here with no other object except in what they consider the interests of justice and fair play, to tell you that Mr. Morland has done nothing wrong so far as they know. I am going to do a thing that I should imagine has never been done before, namely, call two witnesses for the defence to prove exactly the same as the only evidence given against Mr. Morland for the prosecution—exactly what Lord Plender has said, and exactly what was said, if he will allow me to say so, by one of the clearest-headed witnesses one has ever heard, the gentleman who went into the witness-box last, Mr. Manning. He was asked: "Would you have signed this balance sheet in 1927?" Members of the jury, I am going to ask the same question of the heads of the accountants' profession. I am going to ask Mr. Morgan, who will say "Yes." If it is necessary to prosecute men like Mr. Morland, then a very large building will be required to try accountants! Surely, if Mr. Morgan comes into the box, representing a great profession, and says: "I can find nothing wrong with those accounts in 1926 and 1927; I would have signed them"—If you think he is coming here practically to plead guilty himself to a criminal offence—

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you must think he is a brave man. The only difference in that witness-box between Mr. Morland and Mr. Morgan and Mr. Hill, and anybody else who may be called, is that Mr. Morland goes into the box to say. "I did it; I know of no wrong," and sitting behind him will be a warder with a chain. That is all. The other gentlemen will come and say: "We would have done it; we see nothing wrong," and they are free. Lord Plender said almost in terms that Mr. Morland had done nothing wrong. But Sir William M'Lintock, the gentleman who knows this case from A to Z, went into the box, and if there was anything in the facts of this case which made Lord Plender's observations not applicable to Mr. Morland, then was the chance to show there was a difference. Other accountants were called, but not one of them has ever said one single word criticising in any way the conduct of Mr. Morland.

What it really comes to is this, the R.M.S.P. was suffering, as every company in the world was suffering, not from bad management, but from the depression existing throughout the world. I suppose it is true that if Mr. Morland had done that which the Attorney-General seems to suggest, if he had said to them in 1921, "Your position is magnificent in the sense that you have got endless reserves and millions of pounds of assets, but I tell you you are living on your own fat. You are drifting to your own doom," the biggest shipping company in the world would have been ruined. Is the Attorney-General really meaning that the duty of Messrs. Price, Waterhouse & Co. was to go to a distinguished and learned board of directors and say their duty was simply to ignore them and do something which would wreck the company? Members of the jury, we know the tendency of English finance, and I am sure the Attorney-General does not require me to prove it. The big joint stock banks have all large secret reserves. In a year a dividend of 19 per cent. or 20 per cent. might be paid, but there might be a time when there was a big financial disaster, such as took place not so many years ago, when the gentleman who was responsible for it stood where Mr. Morland is standing now. Some of the banks lost very heavily. Suppose the directors had said: "Do not put that right out of your reserves, but go to the shareholders of this big joint stock bank and say you have lost £1,000,000." Do you think that would have been a good thing for the credit of this country? Do you think any auditor in the world could do a thing like that? It is easy to be wise after the event. I am going to say that Mr. Morland is not guilty even of an error of judgment.

I am going to appeal to the Law Officer of the Crown through you to consider, even now, whether it is right that for another hour this gentleman should be allowed to continue in the dock. His lordship told you early in the opening of this case that at any moment you had it in your power to say there is no case against this gentleman sitting there. If you think fit to consider this question, I hope you will remember this that for a man to be acquitted is a great thing, for a man not to go to the end of his trial is a thing he will remember

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with gratitude all his life. If there is anything after the evidence which has been given which leads you to think there is any case for him to answer, of course this case will proceed, but I urge on you, either now or when you have heard his evidence, to consider whether you think it is right that a gentleman of his position should remain in the dock another hour. When you have heard Mr. Morland's view, and, if you think fit, the other gentlemen I am going to call, you will say without fear that there has never been one word which could properly be used either against Mr. Morland's honesty, integrity, or his business ability.

## Evidence for the Accused Mr. H. J. Morland.

HAROLD JOHN MORLAND, examined by Sir PATRICK HASTINGS—I am a Fellow of the Institute of Chartered Accountants, and I have been a partner in the firm of Price, Waterhouse & Co, since 1907. I was appointed auditor of the R.M.S.P. about May, 1919, and audited the 1918 and later accounts. Although I was the auditor and signed the accounts, the clerks who assisted me were employees of Price, Waterhouse & Co. The three or four hundred guineas went to the firm in the ordinary course, and I received my share as a partner. It worked out at about £20 a year after I had paid taxation.

Did you ever have any discussion with your co-defendant, Lord Kysant, upon any of these accounts?—No.

Did it ever enter your mind that that board of directors was not as fully conversant with the financial position of the R.M.S.P. as was Lord Kysant?—I did not know anything about the position of the other members of the board.

Did it ever occur to you, or did any one ever suggest to you, that Lord Kysant was the only person who knew the facts?—Oh, no.

Did you yourself require to be inserted, in the profit and loss account for the year 1925, the words "adjustment of taxation reserves"?—The words were suggested by me.

Why did you select that phrase?—I thought it was the best phrase to use; it was a phrase in common use, and to my mind it expressed exactly what I wanted to express.

Had you any sinister motive at all in selecting that phrase?—I selected it simply because I thought it gave the information that ought to be given.

In the years 1926 and 1927, did you use precisely the same phrase?—The same words. The words were in when the accounts came to me for audit, because they had been copied from the accounts of the year before.

And in respect of those two years, in your opinion at that time, and now, were the proper matters brought into the profit and loss account?—Yes.

## Evidence for Defence.

Harold J. Morland

Did you at any time consider that you were guilty of any lack of duty in certifying those accounts?—No

Do you know now in what respect you have acted improperly, if you have?—I have not really heard any suggestion to that effect.

We know that Sir William M'Lintock, at a later stage, was asked to investigate the accounts. Did he ever ask you for any information, or make any inquiry of you as to what you did?—He never came to me. His clerks and mine were in communication with regard to some figures.

Did you give him any information he required?—Yes, we put all our papers at his disposal.

Did he ask you for information or suggest that anything you had done was improper?—I never met him until I saw him at the Guildhall.

It was suggested by Mr. Cason that at some time he told you that he did not much like one of the items about the bonus, and he said that he thought he understood you to say that neither did you. Did you ever make any such statement to Mr. Cason?—He came to me—whether on his own behalf or because some one had queried it I do not know—to ask if the two bonus dividends for Nelsons were really dividends or whether there was anything in the name “bonus” which rendered them improper to be included in the profit and loss account. I told him that they were quite proper to be included.

Did you ever have any reason to dislike it?—Not the least.

Have you ever at any time had any shareholding or any interest in the Royal Mail?—No, I have not.

Cross-examined by the ATTORNEY-GENERAL—It is right that I should accentuate at the very outset certain facts which are in your favour. It is a fact, is it not, that you had no financial interest as to whether a dividend of 5 per cent. or any other dividend was declared?—No.

So far as the subsidiaries are concerned, you would have no knowledge of them?—None, beyond what was in the published accounts, *i.e.*, the audited accounts, which came to me.

The first step is the preparation of the accounts, and with that you are not concerned?—That is an internal matter.

Then the second step is that these accounts, having been prepared, are put before you as auditor?—Yes, after they have been to the board in this case.

We have been told, both by Mr. Cason and Lord Kylsant, that in the course of the year 1926, when a deficiency was probable, an estimate was made and Lord Kylsant told Mr. Cason to ascertain what reserves they had to meet deficiencies?—I heard that.

You knew nothing about that at the time?—Nothing whatever.

You did not know that they had started out with the set idea of utilising reserves to meet deficiencies?—Oh, no.

Neither, I presume, did you know that in the year 1926 the E.P.D. portion which was going to be taken moved up from £350,000 to £550,000?—It was £550,000 when it came to me.

You knew nothing about that being moved up by the £200,000?—No.

You would not concern yourself with the effect which the company's

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reports are having on the public mind?—That has nothing to do with the auditor

With regard to the year 1929, do you agree that there were some guarantees which the company were asking the Treasury to extend?—Yes.

If the Treasury did not extend them, the company was in this difficulty, was it not, that it could not find the money to pay them?—I cannot say that; I do not really know that. It certainly was not convenient; the company was asking for an extension.

It was much worse than that, was it not; the company was unable to pay its debt?—It is awfully hard to say that. I am not prepared to say it off-hand. The company has very large ramifications, and what it was prepared to pay I do not know.

By the Court—When did you cease to be auditor?—I audited the accounts for 1928, and then when the report was put forward I formally resigned, but my firm was appointed auditors. It was only a change in form.

*Cross-examination continued*—The accounts at any rate show that the R.M.S.P. Company, in the year 1929, was in a serious financial position?—The seriousness of the position was that it had these large capital liabilities which were becoming due. That is clear.

Had the company heavy liabilities falling due, and no liquid assets?—It is not exactly a case of liquid assets.

Well, assets which it could readily liquefy?—I should say that the mistake was in borrowing money on such a short term.

I think it was a five-year loan?—Yes. It was, I suppose, rather too optimistic to think that it would have the money at that time.

That being the position in 1929, there having been nothing exceptional in 1928, may I take it that the position was one which at any rate ought to have given rise to some misgiving in the year 1927?—I do not think that would follow.

Did I understand you to say that you thought that what would be required at that time would be a certificate of profits, for use in the prospectus?—Perhaps I was too hasty in thinking so, but it is what I did say.

You thought that you would be asked to certify the various profit and loss accounts; and, in regard to the year 1927, that you would be asked to certify £737,000?—It never got as far as that; I do not think that was in my mind. I thought that I might be asked to state year by year what were the earnings and profits, after making the necessary adjustment that accountants think it well to make.

If you had been asked to certify, for use in a prospectus, what the figures for the 1926 profit and loss account were, you would have been very anxious to avoid misleading the investor, would you not?—Oh, yes.

First of all, you would have altered the build-up of it, would you not?—I think so. We nearly always say that the profits given in a prospectus are the profits after making adjustments, whether large or small.



## Evidence for Defence.

Harold J Morland

Would you mind telling me, as an illustration, what you would have done with the figure of £550,000 (in respect of E.P.D.)?—If I were being asked to certify the profits that the company earned in the year, it could not have been included.

By the COURT—In that year?—In that year, my lord.

*Cross-examination continued*—What would you have done with the £175,000 income tax reserve?—Nearly every certificate for a prospectus leaves out of account taxation altogether.

If it is necessary to present a true picture to a prospective investor, why is not it necessary to present a true picture to a shareholder?—Because the circumstances are quite different. What a shareholder wants to know is what his company had done during the year; and that includes all these items that have been properly brought in.

Do you think that when an ordinary intelligent member of the public or shareholder, but one who was not a specialist, looked carefully through the accounts for 1926 and 1927 he would have a true picture of the company's position?—The balance sheet gave him a perfectly true picture of the company's position.

It is very important for a shareholder to know, among other things, what current earnings his company is making?—I do not see why.

After all, the value of assets lies in the fact that they have an earning capacity?—I agree.

Do you not think now, in the light of after events, that those profit and loss accounts would leave the ordinary intelligent shareholder under the impression that so far as earning capacity was concerned, all was well?—No, I do not think that necessarily. I think anybody who read the accounts would see that there was no statement whatever about earnings.

Do you agree that one of the most material circumstances which every shareholder has a right to know is the earning capacity of the company?—Of course I do not agree with that.

With regard to the utilisation of secret reserves to level out inequalities. If it has been done over a series of years, if substantial amounts have been used, and if it is going to be continued, the auditor ought to insist, should he not, that a clear indication is given to the shareholders?—I should say in general that if there is a large reserve which has not been put aside for any particular purpose it ought to be disclosed from the first. It is of the same nature as transfers to general reserve. It ought to be put to general reserve.

There does come a time, does there not, when, if you are going to utilise reserves in a profit and loss account you must say so?—It is a question of degree. I am not quite sure how much it is time and how much it is size.

In your view, had that time arrived when in the year 1926 you made your report in respect of the year 1925. I select this year because this is a time you put in the words "adjustment of taxation reserves"?—I do not think what was in my mind was that any time had arrived, but here were large amounts coming year after year, and it was time they should be described.

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By the COURT—I should like to know at some time why you thought so at that time?—My idea in putting in those words was this. In that statement which begins “Balance for the year” you have two large amounts mentioned—dividends from allied and other companies, and, on the other side, depreciation. In the second year you had large sums coming in from another source, not non-recurrent, but recurrent, which were quite as important to the company as amounts which were coming in from allied and other companies. If you have got three things of practically equal importance, it seems not a very good method to mention only two of them and leave out the third.

*Cross-examination continued*—I quite follow that; if you say they were recurring, but they were recurring with this qualification, were not they, that the duration of time for which this source of supply could go on was strictly limited?—I did not know when it was going on; it could not go on for ever.

It is abnormal, is it not?—Yes.

By the COURT—It is an abnormal thing which the shareholders ought to know if they are to obtain a true and correct picture of the state of the company's affairs?—I thought it was desirable. I do not think I could put it higher than that.

Mr. Morland, you have a sort of judicial duty here. You have to certify as auditor, and on you depends the certification of accounts?—You put it high, my lord, calling it a judicial duty.

Well, I will say quasi-judicial?—Yes, my lord.

*Cross-examination continued*—And you are not the servant of the directors?—No.

Part of your duty is to see that the shareholders are to be protected?—Oh, quite.

By the COURT—You are not infallible, but you have that duty?—Certainly.

*Cross-examination continued*—You would have been very reluctant to sign the accounts without the words “adjustment of taxation reserves”?—Having made the suggestion, yes.

By the COURT—In 1924 the words were not there. Might not the words of 1924 appear to be rather misleading?—I think, looking back, if I may say so quite frankly, I am rather sorry I did not make the suggestion in 1924, because the amount brought in in 1924 was larger than in 1925.

*Cross-examination continued*—Referring to the statement known as Exhibit No. 21, in each of the years 1921 to 1926 inclusive, was the company, including its gross earnings, less expenses and depreciation, and including dividends, running at a loss?—I think there is a possible exception in 1923.

Is this the position, that from 1921 to 1926 the company had never earned anything like enough to pay its debentures?—That depends, again, on what you mean by “earned.”

I mean earned, after depreciation?—That is quite true if you mean earned in the ordinary sense of the word.

## Evidence for Defence.

Harold J Morland

And in those six years it expended very large sums of money in paying dividends?—It paid regular dividends.

If the shareholders had realised at that time what the true position of the company was, and what it expended in carrying on from 1921 to 1927, do you think they would have been very seriously disturbed?—That is not a very easy question to answer. I should doubt if they would. The chief thing a shareholder wants is regular dividends, and that he had had all the time.

What he wants is not merely dividends, but assurance or security that he is likely to go on receiving them?—That is what he never gets in an industrial company.

Mr. HENRY MORGAN, examined by Mr. STUART BEVAN—I am president of the Society of Incorporated Accountants and Auditors. I have had the material documents brought to my attention, and understand practically the whole of the facts of the trial.

You have heard the different amounts in question in the case of income tax fund, excess profits duties fund, and corporation profits tax. Were they properly brought in or improperly brought in?—In my opinion they were properly brought into the balance for the year as the profit available for dividends.

In your opinion, on the facts as known to you, was the balance sheet properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown by the books of the company?—It was.

With your knowledge of the position of the R.M.S.P., as it was in the years 1926-27, would you, as auditor of that company, have signed the balance sheets in this form?—I should.

Cross-examined by Sir WILLIAM JOWITT—Take the year 1927. You see there a balance for the year, including dividends on shares in allied companies, adjustment of taxation, &c. Supposing you had been asked for the purposes of a prospectus to make yourself responsible for a statement on those lines—that is to say, a certificate put exactly in that form that a balance for the year has been £697,456, would you have done that yourself?—I should want to put the balance available for dividend for that year. I should want to make it quite clear that it was balance available for dividend, because, of course, there is a tremendous difference between profit available for each year and the profit earned in the year, calculated according to the ordinary commercial standard, and, of course, obviously here, this cannot be profit earned in the year.

Do I understand you to be saying that there is a distinction between "balance for the year" and "balance available"?—The amount of profit available for dividends in each year need not necessarily coincide with the profits actually earned in that year calculated according to commercial customs.

That is, there is a distinction between a profit for the year and a profit available for the year?—That has become available for dividends during the year.

Would you have consented to have put your name on a prospectus containing the phrase we have been discussing?—Well, sir, it appears to

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me to be merely repeating what has been stated in the accounts for each year. Now, as an auditor, I should not consider myself responsible for the extent of the disclosure in the profit and loss account. But it is a sort of certificate that I should not like. I should like it to have been explained a little further that this was the amount that became available for profits during the year.

You would say "No, if you want me to certify on these lines, I won't do it, but if you want me to certify the balance for the dividends in the year, perhaps I would"?—That is it, exactly. I would if I signed the balance sheet.

HENRY LANCELOT HINGSTON HILL, M.A., examined by Mr. STUART, BEVAN—I am president of the Institute of Chartered Accountants. I have been in practice as an accountant for twenty-seven years. I am familiar with the question which has arisen as to the inclusion in the profit and loss account in 1926 and 1927 of sums drawn from income tax, excess profits duty, and corporation profits tax. In my view they were properly brought in. I think the phrase used quite suitable.

Cross-examined by the ATTORNEY GENERAL—You agree with me from the accountant's point of view this matter is a matter of degree?—Exactly.

Entirely a matter of degree?—Yes, I think it is.

Whether you are right or wrong in law, we are not debating in this case, because, as I say, this is not the proper arena, but, in fact, transfers from a reserve fund are sometimes brought into a profit and loss account without any notification at all?—Yes, that is so.

Then there comes a stage—whether, as Mr. Morland said, it is reached as a matter of time or by the size of the amount—there comes a stage when some indication must be given?—Yes, some indication.

Some indication! Does there finally come a stage when there must be not merely an indication but a perfectly precise phraseology when nobody can make a mistake about it?—I should think so; it depends on the circumstances; one cannot generalise exactly.

The Court adjourned.

# Closing Speech for Lord Kyslant.

Eighth Day—Wednesday, 29th July, 1931.

## Closing Speech for the Accused Lord Kyslant.

Sir JOHN SIMON—If your lordship pleases, members of the jury, you will, I am sure, be glad that we have now reached the closing stages of this trial, and, close as your attention has been throughout, you must necessarily, in the course of the case, have felt occasionally a little weary if matters already discussed were again put under debate. I have, as you realise, resting on my shoulders at this moment a very grave responsibility, as grave, I think, as any that has ever rested on them in my professional life of now thirty years. You will forgive me therefore if I refer to some things which you may already feel are familiar to you. I desire here to do my duty simply and clearly, and that duty requires that I should, even at the risk of being thought wearisome or redundant, present to you a connected view of this matter, which, if it commends itself to you, I shall invite you to bear in mind until the end.

The first thing which I wish to state to you before we come to any matter of detail, before I attempt to put before you any argument in the nature of appeal, is that you should realise and have in mind that on each one of the three counts of this indictment, both the two counts which affect Lord Kyslant and Mr. Morland, and the third count about the prospectus which affects Lord Kyslant alone—on each one of those three counts three distinct things are necessary to be proved to the satisfaction of each one of you. If it were proved that any one of these three things was, in the judgment of any one of you, not adequately proved to your satisfaction by the prosecution, you are bound in that respect to acquit.

What are these three things? They are three elements in the charge. I do not agree, and I do not think when my lord sums up that he will agree, with the view which was rather suggested at the beginning that, as a matter of fact, if the first of these elements was established the other two would follow almost automatically. The first question in relation to each count is: is it proved to your satisfaction that in a material particular a false written statement has been made? I am going to submit to you reasons why you should think that that would be too harsh a view. I have already taken occasion to point out, and I think my lord here again will confirm me, that, leaving aside for the moment the question of the effect of what is stated, this criminal section under which an accused person may be brought to the Old Bailey and tried as for a crime and his liberty put in jeopardy is not a section which is laying down what is to be the extent of disclosure, what is to be the amount of information given, what is to be the fullness with which details are published. These matters may be very proper matters for a very different tribunal in the course of a civil trial when you are dealing with the subject of monetary liability or compensation, but here

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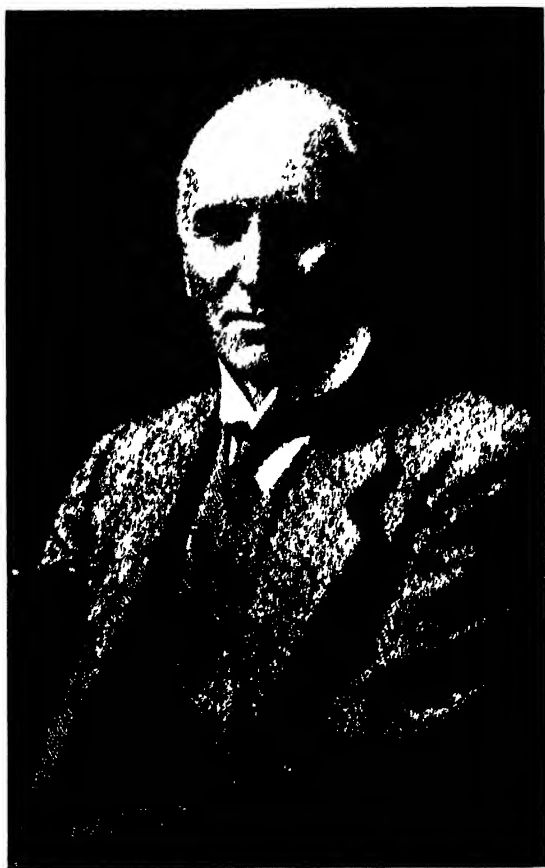
in this Criminal Court, dealing with this section of this Larceny Act, the first issue, as I conceive, is not an issue as to whether it would be proper or wise or good accountancy or good business or more informative to provide additional detail. The question is: is there, in that which has been stated in writing, a material particular upon which you can put your hand and say "That is false"?

Secondly, in respect of each count of this indictment, quite independently of the first point, you have, before you could convict, if indeed any holes could be picked in any material particular in what has been stated in writing, to be satisfied that Lord Kysant, in that which he did put forward as a written statement, knew that what was being said was false

And here I may be, perhaps, permitted to submit to my lord and to you, through him, this consideration. One can well understand that the view might be advanced that this section, when it speaks of falsity in a written statement in a material particular may, and on one construction perhaps would, cover the case not only on what is stated sentence by sentence, figure by figure, word by word, but would cover also what might be regarded as the effect of what was stated. Let me suppose, for the sake of argument, that you have a business man with great affairs who, as a matter of fact, entrusts a good deal of the accountancy side of his business to others. Let me assume that you may have before you a man who, though holding a distinguished and honourable position, may not in every respect have had as clear and pellucid a view of every detail of the income figures of his business as some others, as the Attorney-General would say in his pleasant way, not a senior wrangler. If indeed the question was: Here is something which you have put down in black and white and it is a lie; you will not hear me stand up and say: "Oh, but he did not know that it was a lie." But if what you wish to imply is that we must consider the general effect of this, not the words used, then the question I think does arise very importantly indeed as a fair question: "Aye, but even on that assumption, is it proved that the defendant knew that this which has now been analysed for ten days in a Court is false?" Your lordship sees my point, I am sure, and I think it is a rather important consideration.

MR. JUSTICE WRIGHT—Yes, it is a very important matter for the consideration of the jury.

SIR JOHN SIMON—You will remember that when Lord Kysant was in the box I was very careful to put to him that question, not in any way suggesting to him an answer or leading him, and I daresay you will remember my phrase. I said: "If anybody could pick holes in that statement, the prospectus would tell the jury the answer to this question: 'Did you know or realise that it could be in that way treated as false, and did you know that what you were putting forward was in that sense false?'" And after all a man on his trial is entitled to have some regard paid to his answer, especially when he is not cross-examined about it, and his answer was. "No. I believed that what I was putting forward was true; I did not intend to put forward what was



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false," and I ask every one of you to attach to that the weight which such an answer deserves

The third element which has to be established in every one of these counts is one of which I am going to say something to you at the end; very little has been said about it yet, but it is vital in this case. Let it be supposed that as the result of all this elaborate preparation it could be shown by the prosecution: "Here is something which is false" I deny it, but let it be supposed. Let it be further supposed that it could be said: "Not only that, but the effect of it is something which Lord Kyslant knew to be false." I deny it, but let us suppose it. This tremendous question remains, and it is essential to any conviction on any count; has that which has been stated been stated with any intent to deceive and to defraud? That means this: is Lord Kyslant a rogue? That is what it means, and no one of you, with very great respect, would be justified in returning a verdict against Lord Kyslant, unless every one of you reaches the conclusion that that is the intent with which it was done

When it was decided to institute these criminal proceedings against these two gentlemen, the view that was then taken was a view which involved these propositions. I am not saying that the Crown is not entitled in the course of the case, when it ascertains more accurately the facts, to change its attack. Certainly, this thing must be investigated from every point of view; but when Lord Kyslant for the first time in his life found himself summoned in order to answer a charge of crime it was manifest that the Crown then put forward a case that what these profit and loss accounts asserted was that the company in 1926 and 1927 had made a trading profit. It is a pure delusion. It is now plain to everybody that, as a matter of fact, whatever this profit and loss account is, it is not a trading account of the company; it is not a representation that the company has made a profit in its trading during the year.

I pointed out to you that when this case was first presented it was made a specific part of the injurious imputation directed against these two gentlemen: "Oh, yes, you say 'Adjustment of taxation reserves'; those words mean small modest adjustments." I again remind you, if that was the view that was ever entertained by the prosecution, it is fatally exploded by their own witnesses.

I am bound to say I am not content to leave the case without pointing out how it has been transformed in the course of this trial at the Old Bailey. I am going to give you three instances. The first is: the Crown and its advisers had the opportunity of studying this material for weeks and months, and after they had had the advice of counsel and any accountants who were called into conference, the Attorney-General, when he comes to these words, "Adjustment of taxation reserves," uses this passage. He suggested to you in opening, and of course he was presenting the view which the Crown then entertained, that the phrase was deliberately prepared and selected and chosen as a phrase, and that it betrayed an uneasy conscience. The Crown had all the accountants of the City of London ready to come and assist them if they



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liked, and you know now that, as a matter of fact, that phrase, whether it is right or wrong, is a phrase which is constantly employed by accountants of the very highest standing. It is a phrase which Mr. Morland, as an accountant of the highest standing, himself suggested, and it was adopted. It was not Lord Kysant's intention. As a matter of fact whether it is a desirable or an undesirable phrase, whether it is an adequate or inadequate phrase, whether it is an apt or inept phrase, it is, and the Crown ought to have known it, a phrase which accountants have often used—that and similar phrases. It is not to be attributed to Lord Kysant. It is not the invention of somebody with an uneasy conscience. You are quite entitled to take the view, and it may very well be how you will regard it, that it would be better to use plainer language. We all learn something from every case, and I daresay some people will learn a good deal from this case, but that is a different thing to coming here at this trial at the Old Bailey and presenting against Lord Kysant this horrible suggestion that it was he who said. "Now we have something here we must be careful about; let us write down, 'Adjustment of taxation reserves'" We now know perfectly well that the whole of that suggestion has been disproved in the course of this case; but I do make the observation that it is a matter which the Crown could perfectly well have ascertained before ever this prosecution was started. I will take the second case. My learned friend on his information, not merely in the opening but as late as the sixth day of this trial, was still, I regret to observe, under a complete misapprehension, which those assisting him I think might have cleared up. Let us just see what the imputation was, because it was a deeply injurious one. It begins by the suggestion that in the year 1927, in order to qualify himself for his commission—and that is the sting of it—Lord Kysant brought in from the Pacific Steam Navigation Company a dividend of some £60,000. The suggestion was that £10,000 of it was paid in cash, and £50,000 of it was not paid in cash, but that the balance was used in an account to subscribe for shares in the White Star Line at 2s. paid, leaving, as the Attorney-General was instructed to suggest on the sixth day of the trial, in the year 1927 a great liability overhanging the company at the very moment when Lord Kysant was therefore qualifying himself for his commission. This was being developed with so much art that I interrupted and said that there was a misapprehension about it. The Attorney-General, however, quite rightly put what he understood was the position. The fact is, first of all, that that which is being quite inaccurately referred to never occurred in the year 1927 at all, and, secondly, it had nothing in the world to do, and could not have anything to do, with Lord Kysant's commission. In that connection I would refer your lordship to Mr. Manning's evidence, where he said: "The dividend which was declared by the Pacific Steam Navigation Company was credited in the books of the Royal Mail Steam Packet Company on the 13th June, 1928." That is clean outside the year of charge altogether and has no more relation to Lord Kysant's commission than have my rees in this case. That is after the 1927 accounts have been passed and everything has gone through. There is absolutely nothing in the point at

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all. The learned counsel for the Crown, Mr. Pritt, who, re-examined, recognised that a blunder had been made. We all make blunders. The world is full of blunderers. There are far more blunderers in this world than there are criminals.

Now I will take the third instance. You will recollect, I am certain, the story about the Nelson dividend, altogether £300,000, which came in in the form of bonus, which is nothing more than a lump dividend, £200,000 in one company and £100,000 in the other. I find in the shorthand notes a particularly injurious passage where the question was asked: "It might have been at that time, and probably was, very inconvenient, if not impossible, for the Nelson companies to find the cash to pay the cash bonus." What does that mean? The suggestion is being made, of course in all good faith, but quite mistakenly, that that £300,000 coming from the two Nelson companies was not paid in cash, and is not represented by cash. I call your attention to Mr. Cason's evidence where I put this question to him: "Q. There is one further question I should like to get answered on this subject before I go to other matters. Tell the members of the jury this: So far as your evidence goes, and so far as you know, had the Nelson companies, the two companies, the money to pay the £300,000 in 1927?—A. Yes. Q. £200,000 from one and £100,000 from the other?—A. Yes." There is not the slightest doubt, when one looks into the matter, that the Nelson companies have been exceedingly prosperous, they have made a very large sum in profits, and there is just this question which occurred to the mind of Mr. Cason, namely, whether or not it was technically right, when they were paying a very large amount to the Royal Mail Steam Packet Company which held Nelson investments, to pay it in the form of bonus, or was it not more correct to pay it in the form of declared dividend of so much per cent. I put that very question to Mr. Cason, because I wanted to see whether that was not the point, and Mr. Cason said he took advice as to whether it would be technically right to declare an ordinary dividend and distribute the rest by bonus or not. Mr. Cason agreed it was nothing more than a lump sum bonus; and when I asked him: "You satisfied yourself that that was technically correct?" he said "Yes." In reply to another question Mr. Cason said he had asked Mr. Morland's advice with regard to it. Mr. Cason never entertained any doubt about the matter at all, and it had nothing whatever to do with Lord Kyslant.

I do want you to realise the enormous danger that a man runs with all the panoply of the forces of the Crown arrayed against him, however cleverly they may be deployed and generalised, when it is possible for a mistake of that sort to be made in these circumstances. I can well understand the view being entertained after an event, in 1931, that there is a great deal to be said for a larger and fuller statement. That is a question of the degree of disclosure. As a matter of fact, between the time when these things occurred, which you are investigating, and to-day an Act of Parliament has been passed—the new Companies Act of 1929—to deal with a wider disclosure of secret, internal items. As a matter of fact,

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even under the new law, it is not called for. My lord has pointed out that, of course, here we are not discussing the proper construction of the Act of 1929, but what is perfectly certain is that at the dates which you are now investigating, 1926 and 1927, there was nothing whatever in the law to call for anything of the kind. The Larceny Act says: "You shall not play the rogue when you are making written statements, whether in the form of a profit and loss account or a balance sheet, or a prospectus or anything else, by putting forward statements which are untrue in a material particular to your knowledge." I am perfectly content to accept that burden. It would be a very grave injustice if it were supposed that that is the same thing as discussing how much disclosure, it may be in the future, it would be right and proper to make.

With regard to what is called income tax credits or reserves, let us suppose that the whole of the investments of the Royal Mail were in one single subsidiary, and that that subsidiary declared a dividend which, gross, would be £100. Of course, the company which is declaring it, the subsidiary, would deduct tax and would therefore discharge its obligation if it paid not £100 but £80. Now, in those circumstances, if everything else was square, it is possible for the Royal Mail Steam Packet Company to declare a dividend of £100 and to pay £80. The point which I do not think was quite fully followed was this. One way in which you might state these facts would be to say Dividends from investments, £100, and then to keep an income tax ledger in which you would debit yourself on one side with the £20 which you had to forgo, because it was retained by the subsidiary, and you would credit yourself, on the other side, with the £20 which you would keep back when you declared your dividend. If it were done in that way, what really happens is that in your income tax ledger on one side you are debiting yourself with something you do not really receive in cash, because you are only receiving the dividend net, and on the other side you are crediting yourself with something which in that ledger you are treating as received, because you do not pay away the gross, but only the net. If that is done, the real result is this, that when you take Exhibit No. 21 every figure on it is all right. I am not complaining of the figures at all, but as a matter of fact they are stated in a way which produces, or might easily produce, a false impression. They are stated on the one hand as a case in which income from investments is stated net and not gross. If you state the income from investments net, then you do not need to bring in the special credit, due to the fact that when you pay dividends yourself you deduct at the source the income tax. You need only the special credit, so far as it arises, from deducting income tax when you pay dividends, in order to set off against what I might call a debit which is really the money which is not received in fact when you receive your dividend from your subsidiary. If you were to say that the dividends which had been declared bring in gross £540,000, the immediate result is that you would proceed to debit your income tax ledger with the difference, and to that extent to set off the special credit. It really is quite fallacious to treat the special credits as if they are really brought in, unless you treat interest on investments, as I think

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an accountant would treat it, as a gross and not a net figure. The result is that, as things are, it looks as though you were bringing in much larger sums than you really are. The real truth is that your income tax ledger is a ledger in which you set off the sums that are deducted by your subsidiaries before you receive your dividend against the sums which you deduct when you distribute your dividend to your shareholders. I agree it is a subtle point; but, after all, it is necessary in a case of this complexity to appreciate what I am saying. I am not saying that the figures in Exhibit No. 21 are not correct as figures. As Mr. Morland said "They are correct as figures, but I could arrange them in twenty ways for you and they would look very different." They were not drawn up for this case, but they are a very useful form of record to keep before your eyes. Do not let us perpetrate the grave injustice of misunderstanding what they really mean. The Crown is not entitled now to say that, so far as these income tax figures are concerned, they are not figures which are received in the year, carried to profit and loss in the year, and distributed in the year. It is not true that in the year 1926 sums were being drawn out of an income tax reservoir. If such had been the case, the result would have been that at the end of the year 1926 the reservoir would be more empty than at the beginning, and that is not true. As my lord pointed out, when you look at it, you find that at the end of the year the reservoir is fuller than it was at the beginning. So it was manifest to everybody that that was a mistake, and Sir William M'Lintock honestly and candidly said at once: "Yes, I quite recognise, as far as income tax is concerned, those are things which arose in the year; they were distributed within the year."

I am not going to delay you by a long disquisition about excess profits duty, but I do hope that as the result of your patient hearing the matter has now become fairly clear to you. It is absolutely untrue to say that in 1926 and 1927 the excess profits duty transfers were transfers from some former reservoir. I can forgive anybody, whether he is the Attorney-General or an accountant, or whatever he is, for not getting this thing quite right to start with. After all, this is the eighth day of the trial, and it is time to see where we are. Let me make myself quite plain to you. Do not think I am shirking this point. I believe that now this has been looked into it will be found not that it is one of those dangerous points which counsel for the defence would be wise to avoid, but, as a matter of fact, this is the vindication of what has been done, and which Mr. Morland proved. If you look at the bottom of the document you will see there seven figures which show what, in fact, was carried into the profit and loss account. In 1921 nothing whatever was carried into the profit and loss account, but there being about £300,000 which might have been so carried, it is used instead to write down investments. In other words, it created a further internal provision—much better, of course, than distributing it, because once you distribute to shareholders you cannot get it back—you cannot get butter out of a dog's mouth. On the other hand, if you use it for the purpose of writing down your investments, it

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is there in case you need it. That is 1921. As regards 1922, Mr. Manning explained exactly that matter and clarified it to this extent, that they were about to transfer £100,000 to profit and loss account. Now, if you add those two figures together, they amount to £400,000, and, speaking in quite round figures, that £400,000 nearly exhausts the whole of the excess provision which had been made by reserving £2,260,000 for excess profits duty. If for the moment we assume there never had been such a blessed invention as obsolescence allowance, if we assume for the moment there never had been such a thing as deferred repairs allowance, if we assume that this was simply a tax which fell upon the backs of companies when they made excess profits, and made them pay so much for seven years, the situation is this, that the reserve which was made for excess profits duty turned out to be some £400,000 or £500,000 more than it need have been, and, that being so, the years 1921 and 1922 exhaust or practically exhaust that reserve. Where then does the money come from which is found transferred to profit and loss account in 1923, 1924, 1925, 1926, and 1927? Because, mark you, from the beginning to the end of this case the statement has been made and reiterated and insisted upon that this has been in 1926 and 1927 a drawing away from a reservoir of reserves. Now look what it really is. It has absolutely nothing to do with it. The Government repaid certain amounts. Strictly speaking, it is not so much repaying as paying. There was a payment by the Government to the company in 1923 of a quarter of a million pounds. Governments do not draw cheques, but they give you things called Treasury warrants, or something of that kind, and you put it through a bank. Having paid a quarter of a million pounds in 1923, £100,000 of it was taken to the profit and loss account. In 1924 the Government paid £390,000, and there was transferred to profit and loss account £330,000. In the next year, 1925, there was no actual further return, but the deferred repairs claim was agreed, and therefore the accountants knew in the year 1925 that it was perfectly right to transfer £300,000. In 1926 the Government paid a further £270,000, and there is transferred £550,000, and in 1927 they paid £9000, and there is transferred the balance. You must add to those figures which the Government actually paid a sum of which you have heard, of £551,000. Adding up those cash repayments, you will find it comes to £920,000, and adding to them the £550,000 you will find it comes to £1,470,000. That £1,470,000 is practically the same amount as was transferred to profit and loss account from 1922 to 1927. Now that you understand these accounts, you will see in the years 1922 to 1927 it is not true to say that they were eking out their profit and loss account by drawing on an earlier reservoir, but, on the contrary, they were receiving year by year from the Government great sums which were distributable, and which were perfectly properly distributable, as profits. I am at a loss to understand the difference between receiving in the year 1924, let us say, £390,000 paid by the Government, and receiving £390,000 bonus or dividends from anybody you please. I have not had the advantage of being a Senior Wrangler; I am only a man who tries to understand figures;

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but I do not understand at this moment what is meant when it is suggested by eminent persons who are presenting this case for the prosecution that in 1926 and 1927 this company was feeding off its "old fat." I daresay you remember the Attorney-General's expression. Where does the fat come from? It comes at the time from the Government as a payment; it is flesh. I repeat for the moment the only point remains that after all the Government was not going on doing this for ever. I trust I have established this to your own satisfaction, that it is a complete misunderstanding to say what was said in the opening by my learned friend the Attorney-General when he spoke of those figures in 1926 and 1927 as figures which in no way ought to appear there at all. Why not? Why should not the £550,000 appear where it does? I have not the faintest idea, once the figures are understood, why that should not be so.

MR JUSTICE WRIGHT—About this question of income tax, would you mind telling me if there is anything in the accounts of the company which shows the debits and credits?

SIR JOHN SIMON—I am told, my lord, there is such a thing. It is a difficult thing to follow and not easy to explain, but I am told so.

MR. JUSTICE WRIGHT—It is not in the income tax reserve account?

SIR JOHN SIMON—No, you will find it in Exhibit No. 15. Your lordship remembers that this is a more detailed thing which is kept in the company's offices. If you take the second page of Exhibit No. 15, and look at the right hand side at the top, you will see an entry: "By interest on investments 30th June and 31st December," carrying out a total of £611,798. On the other side, on the debit side, you will see: "To income tax on investments 30th June, £26,000; 31st December, £26,000; £52,000." Please understand I am not in the least challenging the correctness of the figures. If your lordship looks at Exhibit No. 21, you see it is not stated as being a receipt, with the result that you get the credit set against the debit, but it is stated as being the net amount, in other words, you get the £52,000 subtracted from the £600,000.

MR. JUSTICE WRIGHT—I follow. I am not quite sure I appreciate what effect it would have in the result.

SIR JOHN SIMON—It is this. If for the moment we imagine ourselves as recording any income from investments, it is in the right-hand side column, and then there are two items which as far as they go are set off against one another. One of them is the debit, being, in fact, that portion of the gross dividend which is stopped at the source, and one the credit you yourself stop. Those two things are on opposite sides of the account; one is debit and the other is credit. You may leave the debit and credit to cancel one another out. You can speak of receiving your dividends net, or, alternatively, you can speak of receiving them gross, and in that event you must allow the debit against that gross figure to be set off against the credit. If you look at Exhibit No. 21, you have got in the figure, income tax reserves, the sum that the company is credited with, but you have not, as you ought to have, that which is set off against it. Therefore the true accountancy position

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is this: you really ought to regard yourself as receiving from your subsidiaries your interest gross, and you ought then to proceed to debit yourself with that which has been deducted at the source.

MR. JUSTICE WRIGHT—I thought possibly the view might be that your own dividends were quite a separate matter I shall look again at the income tax reserve account.

SIR JOHN SIMON—If I may say so, I think that is in Mr. Manning's evidence, and it is very clear. I was finishing about the excess profits duty, but I think you do see what is the point which we put. If the learned Attorney-General will be good enough to allow me to state the real point, it is that from 1923 to 1927, as far as the excess profits duty figures in the profit and loss account go, they were not drawn from the vintage years at all; they were in fact represented by receipts which the company was getting at that time. Just as it got its bonus from the Nelson Company, a payment to the profits, so it was another receipt of a payment into profits. You have still got to consider the last point I have to deal with, whether or not, in view of the fact that the Government will not go on doing that for ever, you should not give some indication that as a matter of fact these are not necessarily recurring I want to get rid of what I regard as a complete delusion, a delusion which may be illustrated by my learned friend's observation in opening the case, to the effect that these figures ought not to appear at all, they in no way relate to the year; and there are many other passages throughout. I think we have now all reached this plain view, whether it be right or wrong on other grounds, whether disclosure be adequate or inadequate, that it was quite a mistake to suppose that the profit and loss account was being fed from some vintage or ancient source. It clearly was not; it was being fed from sources which, though they might not continually repeat themselves, were perfectly appropriate to be regarded as being associated with a payment in the course of the year.

Now I want to say a word on this remaining view which I am not shirking. The point is made, and, as far as it goes, it is a point of substance and validity: "Well, be it so; we will treat these things, if you like, as things which arise or are associated in the year, distributed in the year; still, they are not the sort of items which would go on repeating themselves indefinitely." To that I think there are two very adequate answers. First of all, as was pointed out, I think, by more than one of the accountancy witnesses, it really is a misuse of language to say that these things did not recur at all, because you see they are spread over a series of years. What is really meant is that they are a source of contribution which is about to terminate. That is true, but there are two answers, I think, which have to be weighed in this connection. The first is the observation which has been made by several of the accountancy witnesses, that it is manifest when you are dealing with a great concern like the Royal Mail Steam Packet Company all sorts of non-recurring or terminal items are coming in. As a matter of fact, in a great company like the Royal Mail Steam Packet

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Company all sort of things which in a way may be regarded as exceptional or non-recurring, or as likely to terminate, are coming in; ships are sold, premises are sold, bonuses are paid, and you have, of course, exceptional losses. You have in mind, I am quite certain, the evidence given by the accountants under cross-examination that, as a matter of fact, in dealing with the accounts of great companies like this a distinction is not drawn by accountants between what have been called non-recurring and recurring items. That, I venture to think, in itself is a quite sufficient answer; but there is a second one, and I mention it because it helps me in the only other part of the case about which I have to detain you. It is that you must not look at the position with the eyes of 1931; you must look at the position with the eyes of 1926 and 1927; and whatever else may be learned from this case when it is finished, I should think you would be satisfied with this, that Lord Kylsant did honestly believe that this shipping business, which had its fluctuations, its ups and downs, indicated by the cycles of trade, was improving. He expressed the view at the time that "Things are mending. We are rising." If that is so, could anything be more unfair than to turn round on him in 1931 and say: "There you are; you ought to have known that things were going down and not up, and if things went down and did not go up, then where were your resources when the excess profits duty repayments were finished?" His answer is a perfectly simple one. His answer is: "I, in common with many another man, in 1926 and 1927, was perfectly satisfied that I had got over the last ten years, a cycle of good years and bad years, and I believed that there were indications that this company would be gradually restored to its normal prosperity."

Lord Kylsant was not doing what people sometimes do—distributing to-day what he hoped to get next year. There is not a penny that has been distributed here which was not already available. One knows of the sporting and sanguine gentleman who is sometimes tempted to take money which he is not really possessed of, and go in for a gamble, and, having backed a winner, hope to return the money he has borrowed, and to make a fortune thereby. That is not this case at all. There is not the slightest ground here for suggesting that anybody has anticipated any single item of receipts. Every receipt in this case had been received, was properly distributed, and was not distributed too soon. When it was suggested: "But you know you were not going to live on the Government's obsolescence profits for ever," the answer was: "No, and I was not going to stay in the trough of the wave for ever."

I wish now to refer to a statement that was made by Lord Kylsant at a meeting on 26th May, 1927, which is contained in Exhibit No. 114. It seems to me that this document is perhaps the best available document to show what was the state of Lord Kylsant's mind at the time when this profit and loss account was put forward. We all realise how fatally easy it is to argue backwards. One is always meeting people at the present time who tell one how foolish people were four years ago; and that applies both in business and in politics. At that meeting in May,



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1927, Lord Kylsant said. "The accounts reflect the abnormal conditions which obtained last year"—and they do—"as the result of the General Strike and the prolonged coal stoppage. Whilst indications in the earlier part of last year pointed in the direction of a general recovery from the protracted depression in trade, all hope of this was frustrated by the industrial troubles which followed. Operating expenses were substantially higher by reason of the extra cost of coal and otherwise, whilst exports of manufactured goods diminished." He is not presenting to the world a glowing picture. Just look at the way he deals with the situation. What he said was what the accounts disclosed. He added: "There is a widespread feeling that the worst is over and that we may now justifiably look forward with confidence to more settled and prosperous times." Then he said: "I am personally a believer in the principle of trade cycles, which throughout my business life have usually been of seven to ten years' duration. It is now just over seven years since the slump began, and I incline to the view that the upward movement, although as yet not very pronounced, has already begun," and apparently others in the audience agreed with him.

I would just like you to look at the observation of Sir Fortescue Flannery, who is a shareholder, and one of the very people who is said to have been deceived by these accounts. He said: "It is true we did not have a good year from the point of view of profit and loss"

I have never taken the view in this case that the prospectus, rightly understood, really involves a different question. Let us look at it for a moment. If you look at the prospectus you will find that the language used in the prospectus, on the second page, is this: "Although this company, in common with other shipping companies, has suffered from the depression in the shipping industry, the audited accounts of the company show that during the past ten years the average annual balance available (including profits of the insurance fund), after providing for depreciation and interest on existing debenture stocks, has been sufficient to pay the interest on the present issue more than five times over." It is an absolutely accurate statement. You may say, if you like, that in the early part of those ten years trade was unusually prosperous, and that in the latter part the company suffered from extreme depression. If it is said: "Oh, yes, but if you state the average of something over £500,000 a year, whereas at the end of the time the figures are below the average, you really ought to give some indication of it," the answer is that the prospectus does give an indication of it, for it begins by saying that the company has suffered from the depression in the shipping industry. For my part, I can see no difference whatever between a cricketer saying in the middle of the season: "My average is 50, but recently I have been very much out of form," and a company saying: "My average is £500,000, but recently the company has suffered from the depression in the shipping industry." Are you really to treat people who read these documents as a lot of babies who did not know that not merely the shipping industry but other industries were, as a matter of fact, gravely depressed in the year 1928? Is it tolerable that

## Closing Speech for Lord Kyslant.

Sir John Simon

in these circumstances Lord Kyslant should be put in a criminal dock and prosecuted on such a matter when it is manifest, if you read the document, that the document is not stating anything which is false, still less anything which is false to the knowledge of Lord Kyslant, and with the intention to mislead or deceive any one? What could be fairer than to take a period which illustrates the whole cycle of trade? What could be better than issuing this at a time, as I heard my friend say, when the dividend had been decreased, and £150,000 had been taken from reserve? What more are you to do? If you are going to state an average, then state it; and it is quite truly stated in the way in which it is done. The consequence is, therefore, that the statement that is made in the prospectus is absolutely correct; and it would be a most shocking result, in my humble submission, to attribute to 1928 the sad knowledge which we possess in 1931 Lord Kyslant, when he put forward this document, was putting what he believed to be true, and what he desired to state quite honestly.

The prospectus deals with the issue of second debentures in the company. The claims of the holders of those debentures would come in front of any ordinary, or preferred dividend. The only thing in front of the holders of those debentures is the first debentures. Look at the front sheet of this prospectus, and you see it there;  $4\frac{1}{2}$  per cent. debenture stock, £1,400,000. That, no doubt, would have to be met, both as regards capital, if it came to that, or as regards interest, in priority to the second debentures. Then there comes 5 per cent. debenture stock, £3,100,000, which is now being enlarged, as you know, to £5,100,000. There is nothing whatever in front of these second debentures except the first debentures. And what is there to protect them, members of the jury? Just turn once again to the balance sheet for the year, 1927. Look at the top item on the right hand side. "Book value of fleet, investments in allied shipping companies and other allied companies, £16,366,000." Surely, if anybody is considering an investment that is the figure which is tremendously important. When you further know, as a matter of fact, that the book value of the fleet has been written down with unnecessary severity, you realise that, as a matter of fact, these debentures have not failed to pay their interest. There is no reason whatever to say, as far as the evidence in the case is concerned, that they are not covered and more than covered. The situation of the R.M.S.P. was canvassed and discussed in all sorts of quarters, but when Sir William McLintock was called in to make a report, what is the value which he puts upon the security upon which these second debentures rest? He says that when he made his report and valuation, he thought that a twenty years' life (that is assuming you take 5 per cent. depreciation) as the basis of the combined fleet, which of course includes the subsidiaries, was £15,000,000. The £15,000,000 is really comparable with the £16,000,000 appearing in the balance sheet, for this reason that the £16,000,000 includes, first, the ships that belong to the Royal Mail Steam Packet Company, and, secondly, the investments that the Royal Mail Steam Packet Company

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has in the subsidiaries So that there was an enormous block of solid value lying behind these debentures. Is there really any solid reason for saying this is a case in which a criminal charge should be investigated—I will not say investigated, but which should result in a verdict against Lord Kysant?

You will realise, of course, that this criminal prosecution directed against Lord Kysant and, of course, Mr. Morland, is an investigation in this Court of an aspect of this matter which, it is suggested by my learned friends, constitutes criminal liability. It would be idle to shut one's eyes to the fact that, apart altogether from that, there is always the possibility of a discussion arising elsewhere on what is called civil liability. I make no sort of admission—I see no reason why I should—but you must remember that distinction. Lord Kysant had colleagues on the Board. If civil proceedings arose, those gentlemen might very well find themselves made defendants along with Lord Kysant, and I think you will appreciate that those gentlemen, consulting their own proper interests, may well desire to be protected at this trial. How anybody who realises who those gentlemen were, and what names they included, could imagine that they were gentlemen who were mere guinea pigs, leaving Lord Kysant to do what he liked and merely drawing their fees, passes my understanding. But Lord Kysant here in this Court is prepared to answer for his own responsibilities. You have not seen him trying to shift his responsibility on to the shoulders of anybody else. He is prepared to take his own responsibility at your hands here and now.

The third element in this case which must be proved to the satisfaction of every man and woman among you is this. that in those matters Lord Kysant is a rogue. To issue things which are false, knowing that they are false, with intent to deceive, with intent to mislead, is to be a rogue, to be unfit to have the respect of decent men. Members of the jury, in this Court before to-day there have been directors in that dock against whom it has been proved that they duplicated documents, and by that means raised money from different people fraudulently and corruptly. That is not this case. In this Court before to-day there have been directors, and accountants too, who have been shown by the evidence in the case to have been engaged in falsifying accounts, making entries that were not true. That is not this case. In this dock before to-day there have been directors of whom it has been proved that they have been squandering the capital resources of their company instead of limiting themselves to distributing that which was properly distributable. That is not this case. In this dock before to-day there have been directors against whom it has been proved that while they were telling a smooth tale to the public they were secretly realising their investments and leaving others to bear the burden. That is not this case. I cannot imagine greater proof of honesty than this, that Lord Kysant, who knew everything, apart from the details of the accounts, in respect of this very prospectus, this very issue of second debentures, subscribed his own money and authorised applica-

## Closing Speech for Lord Kylsant.

Sir John Simon

tion on behalf of those for whom he was trustee. If you say, indeed, he is a rogue, he is the meanest rogue that ever was produced in a Court of justice; but I ask you to take a different view. I ask you to take this view, that having been put through this torture—and, I think you will agree, borne himself like a man—Lord Kylsant is now entitled at your hands to a verdict which says that in this matter he has been an honest man.

## Closing Speech for Mr. Morland.

Sir PATRICK HASTINGS—If your lordship pleases: members of the jury: There is one matter I particularly want to mention to you, because I omitted it in the observations that I made to you yesterday, and I think it is a matter which is really worthy of your consideration as a pure question of fact. Except for the moment when the Clerk of the Court read out the charge, I am not quite sure that it has been brought home to your minds that the charge against my client, Mr. Morland, is that of being an accessory or aider to Lord Kylsant in that which it is suggested he has done. The point may, I think, become more clear when the Attorney-General addresses you, but at the moment I confess it is not quite clear to me. I am not quite clear what it is that Mr. Morland is suggested to have done. Is it that he put in the words, "Adjustment of taxation reserves," or is it something else? Because, if so, it is a little odd. He certainly did not aid Lord Kylsant to put these words into the document, because Lord Kylsant did not want them in at all, or he did not care whether they were in or not. Mr. Morland alone put in those words. I still remain, as I have been all along, a little puzzled to know exactly what it is that is suggested against Mr. Morland. His evidence was quite clear. It is entirely a matter for you, but, I should have thought, he said it quite frankly. He said: "I often make suggestions, but only after very careful thought. When I make them, I expect them to be carried out. I made this one." The Attorney-General quite fairly pressed him to know whether he would have signed the balance sheet without them, and he said: "I do not quite know, but if I make a decision I want it carried out, and if it is not carried out I have to consider very carefully whether I will sign the balance sheet at all." If Mr. Morland did that, nobody could suggest that he aided Lord Kylsant to put those words in, because he put them in himself, and Lord Kylsant had nothing whatever to do with it. Members of the jury, when one considers whether or not those words make the balance sheet better or worse, one must remember this—I understand the suggestion is that without these words this balance sheet would be misleading, but these words in themselves are not sufficient. The Attorney-General said: "If you had put that which appears in the year 1928, 'crediting income tax reserves,' that would have been sufficient." You and I are in the same position as the Attorney-General, and, indeed, for this purpose we may all take our own views. You

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may take the view that the Attorney-General is right or wrong, when he suggests that the words "crediting transfers from reserves" would be better than "adjustments." You may take the view that it makes no difference. Any one may make such an assumption; but the question surely that we are considering here is what is the proper meaning to be given to every word that Mr. Morland has used. I do not want to go back and read to you the evidence again, but does it not strike you as odd that no single witness has ever suggested that these words were misleading. On the contrary, an immense number of witnesses have come, and every single one of them, as far as I understand, said in the clearest possible terms that the words are not misleading. The only persons we have had an opportunity of calling with regard to that were members of a profession which is accustomed to deal with accounts and balance sheets, and there has not been the slightest divergence of opinion. If you take Mr. Manning who, if he will forgive me saying so, is perhaps the youngest, although certainly by no means the least clear of the witnesses of professional character whom we have seen, he said in his comparatively limited experience they were the appropriate words to be used in the circumstances of this case. If you go to Mr. Hill, the president of his branch, he says the same. If you go to Lord Plender, who is the leading first witness for the prosecution, he says the same. Is it quite fair that there should remain, at least in this case, this theory that the words which everybody says are the right words—witnesses alike for the prosecution and for the defence—and which were deliberately chosen by Mr. Morland because they were the right words—is it quite fair that they should be criticised now? If the learned Attorney-General's view is right that the words we have in this case, "adjustment of taxation reserves," are misleading, one cannot help pointing out that, if you look at the balance sheet, which he says is right, and if you look at the quotations after its issue, they are equally constant with those which appear the day before. I do not know if the suggestion is that these words "adjustment of taxation reserves" are right for an accountant, but not for an ordinary member of the public. There is not a particle of evidence, not a document—there is nothing or any living soul who says that this gentleman has done anything wrong. On the contrary, everybody, whether you go to the witnesses for the defence, whether you go to the witnesses for the prosecution, whether you go to the voice of the public as appearing in the documents printed at the time, they all say he did right.

If the suggestion is this, that the whole balance sheet in its essence ought to have told the shareholders, through Mr. Morland or with his help, that this company would fail unless trade improved, my only answer to that is, just as I said before, every witness who has been asked says frankly: "If I had been in the position that Mr. Morland was in in 1927, I would have done exactly the same as he did; I would have said nothing." These gentlemen admitted that they would have signed the balance sheet. No gentleman who occupies a great public position is going into the witness-box to commit perjury. If he did

## Closing Speech for Mr. Morland.

Sir Patrick Hastings

so, he would be a figure of scorn to those who trusted him and helped to put him in the position he occupied. How can they say Mr. Morland has done anything wrong? What has he done? What does Sir William M'Lintock say he has done? The Attorney-General no doubt may have some explanation to give you of something that Mr. Morland has done wrong, but it is in the face of the heads of the accountancy profession; it is in the face of Lord Plender, it is in the face of Mr. Hill and Mr. Morgan who have sworn on oath that they themselves would have done the very thing for which this gentleman is standing there in the dock.

Members of the jury, some time ago I suggested that if this action was to result in a verdict against this gentleman you could not get a dock big enough to hold all the accountants who should be tried. I have not got the experience that many of the people have in this Court. There are members of the Bar who practise in this Court habitually, who are here every day, and who see and are accustomed to see men standing in the dock. Quite frankly I am not. I have been wondering since I have been here whether they are not a little apt to forget what we are doing. We are really trying a man for his life. It is life and death to Mr. Morland to be sitting where he is sitting. To me (I do not know how it is to you) it is an unbelievable horror that, night after night, when we have gone home from here, we might have thought: "Here is this gentleman, a man who has held his head as high as any one in the City, who night after night is only allowed to leave his chair by the permission of the law—let out by warders." What can Mr. Morland have done which makes it necessary that when he goes back every night he must know: "When I wake up in the morning, I am surrendering into the custody of warders who will keep me there until I am released by permission of the Court."

Sir John Simon said the case to him is a great responsibility. I agree. To me it is such an awful responsibility that I have struggled to find what point I can deal with and what I can say to help you or him. I can find merely this. There is a gentleman who has, I am told, one of the greatest qualifications, namely, a good record. Mr. Morland is a man who has walked the streets of London, proud of his career, proud of the fact that he could sit beside Sir Gilbert Garnsey and other members of his firm, and beside Mr. Hill and Lord Plender at meetings, and chairmen of companies, and every one of them has been proud and honoured to sit beside him, just as I tell you frankly that I and Mr. Bevan and Mr. Conway are proud to represent him. We have struggled to find what it is we have to deal with and what it is suggested he has done. You have got at this moment in your hands Mr. Morland's whole career and whole future. If you think he is guilty of a crime, you will say so; but if you think, as I ask you to think, that he came into this box a respected and an honoured man, and if you think that he should go out of that box just as respected and just as honoured, that also you will say.

I cannot help you any more, members of the jury, except, in conclusion, to say this. The view I put before you is that it must have

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been years ago, if ever, when into that box stepped a man of the position of Mr. Morland, who has sat there listening to the case against himself, in a case in which he is still wondering what it is. It must be years and years before ever again such a man will go into that box; and I can only beg of you not to be the first jury to say that a man such as Mr Morland must be convicted of a crime.

## Closing Speech for the Prosecution.

The ATTORNEY-GENERAL—May it please your lordship: members of the jury, you have heard both my learned friends in their eloquent and emotional addresses tell you that they were glad that the strain of this case was coming to an end. My object, appearing for the prosecution, is not to endeavour to make, even if I could, either an eloquent or emotional address. I may say, speaking for myself—and I think those who have held my office—that there is no task which, at any rate, causes me personally more anxiety than this task; that there is no strain which I feel greater than the strain I have to undergo, and have undergone, in the past few days. Sir John Simon rightly said, in the course of one of his speeches to you, that there is no question of triumph or victory for an advocate in a case of this sort. The only triumph for which I pray, the only victory I would achieve, is the triumph of right and the victory of justice. My learned friends have told you, and told you quite truly—and I accentuate it here—that these men, the defendants, are entitled to the benefit of the doubt. If you have any doubt in your mind as to this case, whatever you may think about their conduct; if you think that this case has not been brought home, it is your privilege and your duty to say that these men, either one of them or both of them, is not guilty. If, on the other hand, your doubts are allayed, and you are satisfied in your minds, it is then your duty, however stern and unpleasant that duty may be, to say that these men, or one or other of them, are guilty.

There are in this great city in which I am speaking many health services, and ample provision is made for what are called "sanitary services." I have often thought that the function of this Court and your duty to-day is what I may term "a sanitary service." If you think that these defendants are guilty of the crimes with which they are charged, it is your duty to assist in the sanitary services of the finance of this great city. Whatever differences in politics, whatever differences in outlook we may have, we should all agree that, alike in this city and this country, the confidence of the investor, the confidence of the shareholder, and the confidence of the man who is intending to invest in a concern should be restored. Confidence can never be restored unless the shareholder or the investor feels that what is being put before him is a fair, frank, and honest statement of what ought to be put before him. When I hear these emotional speeches, I often wish that that consideration too, could be impressed into the jury's mind. I do not

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mean that I would make use of that consideration to endeavour to persuade you to find these men guilty if you have in your mind any honest doubt. On the other hand, it is so easy to get a great advocate to make an emotional speech in this Court, and so difficult sometimes for the jury to remember that in cases of financial dishonesty there is left a trail of ruin up and down the country. If you think that there was dishonesty here, you cannot doubt but that that dishonesty must have left its mark on many a home. Although it would be utterly wrong for you to let that weigh with you at all in making up your mind as to whether these defendants are guilty, it is a reason which would strengthen and confirm you in doing your duty if you think the charge is brought home.

Now, there are two features in this case which we have had in the evidence in the last few days, which I regret, and with which I am bound to deal. The first matter I regret is the attack which has been made—for it is nothing else—upon Mr. Cason, the chief accountant of this company. You saw him in the witness-box and you realised perfectly well the difficulty of his position. You observed, unless I am wrong, the scrupulous fairness which Mr. Cason exhibited with regard to Lord Kysant. Well, what do I find? I find in the evidence given by Lord Kysant that he says this. I put to him what Mr. Cason said about what took place, or rather what had not taken place, at the court of directors, and he said this: "Many of the questions came up again sometimes after I had left the room, but that, as an account of what happened at the court of directors, is in my opinion absolutely untrue. I am not making any qualification about it. I have a very high opinion of Mr. Cason as far as attending to his job is concerned." It may be at the later stages of this case I will have something to say about it, and it may be not altogether an immaterial circumstance to consider which of those two accounts you prefer.

Sir John Simon, in his speech to-day explained the possibility of civil proceedings, explaining in his own words that these co-directors were consulting their own proper interests. I know nothing about them, I know nothing about their business capacity; the amount of time which they devoted to the affairs of this company I do not know. I do not know of a more serious reflection on a body of men than to say that they are consulting their own proper interests, and in the course of consulting their own proper interests are leaving their colleague and their chairman alone in this dock; it is a serious reflection upon a body of men which, if it is true, implies that they have not a spark of courage. Lord Kysant tells us that one of his co-directors used to cross-examine him as they drove to the City in a motor car. But why cross-examine him? Cross-examination is a means—though not always a very successful means—of getting an answer to the questions which you are putting. At this board of directors, if there had been put forward some document indicating what had been done, indicating what had been transferred from that which, with all due respect to my learned friends, I do not hesitate now to call reserves, what need would there have been for cross-examination? Mr. Cason's evidence is



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that on no occasion when he was present were these matters discussed. These are matters which ought not to be discussed informally at a lunch or in a taxicab; these are matters to be discussed, if ever, at a properly constituted meeting of the board with the chief accountant there, and, for my own part, I should have thought with some document indicating plainly what exactly was being done. That attack on Mr. Cason is an attack which I regret, and which, I submit to you, you will consider was an unworthy attack.

The other matter which I regret is this. In various observations throughout the course of this case criticism has been made or implied upon Sir William M'Lintock. Sir William M'Lintock came into this case with no other endeavour, and with no other instructions, than to advise the Trades Facilities Committee. You heard him give his evidence for the prosecution, and you saw the reticence, and the very proper reticence, which he displayed. You had to wait till almost the last hour to obtain from Mr. Morland the testimony that, having read Sir William M'Lintock's report, so far as he knew, there was only one figure in it which was wrong, and he hesitated to call even that a mistake. For my part I would desire, in view of what has been suggested, to say that I think Sir William M'Lintock, in what he has done and the way he has done it, has rendered signal public service.

Members of the jury, I have no doubt you realise what an important part the accountant's profession plays in modern life. There is no business enterprise—and after all, the whole life blood of this country depends upon the success of its business enterprises—there is no business enterprise that can possibly be conducted efficiently or well unless its accounts are properly kept and properly looked after. I am glad to think that amongst your members there is one at least, I know, who is actually a member of a most distinguished and essential profession. He and you, I know, will not think I am criticising the profession at all if I say frankly in the course of this case I have had some misgivings lest members of it are in the position of sometimes, if I may use the old metaphor, failing to see the wood for the trees. Technical rules of accountancy are admirable things, but they are the letter and not the spirit. It is no good observing merely the letter; the fundamental object of the profession is to ensure that in the documents which are produced a true and accurate account of the affairs of the company is given. If the documents convey to a reasonably intelligent person a false impression, all the technical rules of accountancy may be observed and at the same time the accountants' profession has failed to carry out its primary and obvious duty.

With all due respect to my learned friend, Sir Patrick Hastings, the case which I make here is plain enough. My case is that the circumstances which existed in this case made it essential that the shareholders in this concern should have fairly and truly put before them what the real position of affairs was. You have been told that shareholders have not been called into this box; you have been told, and it is quite true, that lawyers have not come; you have been told that such accountants as have come have expressed a certain view, but I

## Closing Speech for the Prosecution.

The Attorney-General

protest against the idea that this is a matter for accountants or for lawyers, or for any gentleman with technical, skilled knowledge. This is a question for the ordinary man of intelligence in the street to apply his mind to. Shareholders have not come; and why have they not come? Because you, members of the jury, are selected as representatives of the ordinary, intelligent man, and the question is a question for you: would this document have conveyed a clear impression to your minds, had you been shareholders, of what was going on? Do, for goodness sake, let us escape from the idea altogether that the accountants' profession is some kind of mysterious thing, and that you are entitled to use words, in addressing an ordinary shareholder, which might or might not convey a meaning more or less defined to an accountant. That is not the question; the question is, what impression would have been conveyed to the mind of the ordinary intelligent shareholder, and, secondly, what impression was intended to be conveyed? When I heard some of the questions which have been asked, I must say frankly I wondered whether all was quite satisfactory. I heard accountants discussing whether or not things would have been better if, instead of talking about "profits" or "balance of the year," you said "profits" or "balance available"; whether or not some importance is to be attached to the use of the word "&c."; and I think we even got to the stage whether some significance may be attached to the position of the words apart from the words themselves. Then when I asked Mr. Morland a question, suggesting that at least the earning capacity of a company was not an unimportant thing, I was astounded to hear him say. "Why?"

Now, members of the jury, the case which I have made throughout—and which I had hoped that Sir Patrick Hastings had understood after I had opened the case—is this: That certainly by the year 1926 the circumstances of this concern were such that the shareholders had a right to know what was going on, that the words which were used in the accounts for 1926 and 1927, whatever their dictionary meaning may be, whatever their technical meaning may be, were not such words as would convey to the shareholders any picture at all of what was going on. I cannot do better, I think, than accept, from the point of view of City practice, what Mr. Hill, the president of the Institute of Chartered Accountants, said. Sir Patrick said, dramatically pointing at the dock: "Mr. Hill came and said that he would have done it and he would be standing there." I asked Mr. Hill three or four questions in cross-examination. Let me read them to you: "Q. You agree with me from the accountant's point of view this matter is a matter of degree?—A. Exactly. Q. Entirely a matter of degree?—A. Yes, I think it is. Q. Whether you are right or wrong in law, we are not debating in this case, because, as I say, this is not the proper arena, but, in fact, transfers from a reserve fund are sometimes brought into a profit and loss account without any notification of it at all?—A. Yes, that is so. Q. Then there comes a stage whether, as Mr. Morland said, it is reached as a matter of time or by the size of the amount—there comes a stage when some indication must be given?—A. Yes, some

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indication. Q. Some indication. Does there finally come a stage when there must be not merely an indication but a perfectly precise phraseology when nobody can make a mistake about it?—A. I should think so; it depends on the circumstances; one cannot generalise exactly."

Now, that is the evidence called by my friend Sir Patrick Hastings, that is the evidence of the president of the Institute of Chartered Accountants, and it is that test that I will accept in this case. I believe that the test which the law would apply would be a great deal more strict. My lord, in his summing-up to you, or at some stage, may think it right to make some observations about the extent to which the requirements of the law are being observed; but in a case of this nature, where I am dealing with not merely the question of whether the documents are false, but whether there was an intention behind that falsity, it is right that I should accept the test which has been propounded by my friend's witness, and that is the test I accept. I accept the test that sometimes with regard to comparatively small matters, to use my own phrase, levelling out the inequalities, these transfers are made without any notification; there comes a time when an indication must be made; and there also comes a time when there must not merely be an indication, but a perfectly precise phraseology and procedure. If I may borrow my friend's phrase, economy of information no doubt is not the offence which the section under which these defendants are charged is dealing. On the other hand, if you put forward statements without that indication, where indication is necessary, or without that perfectly precise phraseology, where precise phraseology is necessary, the statement which you make does not truly reflect the position of the company, and therefore the account which you put forward is not a true and accurate account. The reason why there is an obligation to give an indication in the one case, or precise phraseology in the other, is because the law requires this, that the shareholders shall have put before them true and accurate accounts.

Presently in the course of my duty, not merely as prosecuting counsel, but as the chief law officer of the Crown, I shall think it my duty to call to your attention certain facts which may, in your view, differentiate, and differentiate sharply, between the case so far as it concerns Mr. Morland and the case so far as it concerns Lord Kylsant. Certainly the last thing in the world that I should desire is that you should lose sight of the fact that there are certain facts which quite clearly and quite sharply differentiate the two cases. The first thing you have to consider is in connection with the accounts for the year 1926, bearing in mind Mr. Hill's test, which I accept throughout, and bearing in mind this little piece of history. Lord Kylsant, in the course of his evidence, said that during those six years 1921 to 1927 the company was not running at a loss. I asked the same question of Mr. Morland: "Q. In each of the years 1921 to 1926 inclusive was the company, including its gross earnings less expense and depreciation, including dividends, running at a loss?—A. Well, I think there is a possible exception in 1923. You will see there is a special debit there of £64,000; what is called the deficit is only £20,000." Then I asked

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him: "Q It does not matter how it is drawn up so long as you bear in mind that all these figures have no regard for the fact that the company in order to carry on its business has to pay the interest on its debentures?—A. Debenture interest is not included there." So that in that year, 1923, if you have regard to debenture interest, Mr. Morland's view would undoubtedly have been that the company was running at a loss. But it is not a question of Mr. Morland's view; it is a question of the plain and the obvious facts of the case.

I am not going to weary you with figures, but I want you to bear in mind this figure, that from the year 1921 to the year 1927 inclusive the company carried on, paying in every year save one a dividend of at least 5 per cent., that the company carried on by the utilisation to the extent of at least £5,000,000 of abnormal credits. I am certainly not going to hold Lord Kylsant guilty, or ask you to find him guilty, because his prophecy has turned out to be false. When he came to prepare his accounts in respect of the year 1927, that would be in or about May of 1928, he would realise that the following year, 1929, was the year in which the company had to meet its obligations to the Treasury in respect of its guarantee. And please note this fact. When I asked Lord Kylsant, "Anyhow, whether the cards were in your hands or not, you had not this card in your hand; you had not the ability to pay what you owed, had you?" his answer was: "As the Treasury did not extend it, that was the difficulty." So that one year—or sixteen months, it would be fairer to say—after the publication of the account in respect of the year 1927, the year in which 5 per cent. dividend was paid, that company had to meet its obligations to the Treasury. The Treasury was free to extend it or not, and they decided not to extend it, and that company was unable to pay its obligations. Now, these are the circumstances. You have the utilisation of that £5,000,000; you have the long series of years over which these very large sums of money had been utilised, or these very large credits had been utilised; you have the fact that Mr. Morland in the year 1925 realised (and this is admitted) that the time had come when an indication should be made. It follows, in my submission to you, that by these years 1926 and 1927 the time had come when, to use Mr. Hill's phrase, if these accounts were truly to reflect the position of the company, perfectly concise phraseology should have been used. The time has come when you must bring home these facts to the minds of the shareholders in this concern—for it is the shareholders' concern, and the directors are in the position of trustees for the shareholders. The time has come when those accounts, unless they were qualified precisely so as to show and to indicate the abnormality of the receipts which were being used for the payment of dividends, would have been false and would have been misleading. I say with regard to the account for the year 1926 that that account would convey to the mind of the shareholder a wholly misleading impression of the situation in which the company was. Can anybody suppose in reading that account that there has been brought into that account to make up that balance such an item, for instance, as £550,000. The evidence of Mr. Morland and

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the evidence of Mr. Hill is: "If you are going to do that sort of thing, the time has come at least for an indication" You will bear in mind what is said in the report of the directors, and you will bear in mind what is said in the speech. My learned friend referred to the fact that some shareholder said, "Hear, hear," when Lord Kysant said at the meeting that he "inclined to the view," I think the words were, "that things were on the upward trend." Sir Fortescue Flannery said it had not been a good year from the point of view of profit and loss. But does not my friend realise how damning that is against his case. The dividends had fallen to 4 per cent., and Sir Fortescue Flannery is saying, "It has not been a good year from the point of view of profit and loss"; he regards 5 per cent. or 6 per cent. as the sort of thing which they hoped for. Members of the jury, that company was never in a position, with its guarantee to the Treasury hanging over its head so near as this, to pay any dividends at all. If the shareholders had known the position, would they not have taken this view—glad though they might be to get their dividend—that this might be the last year, or the last but one, that the ordinary shareholders would ever see the colour of any money at all?

Then in the year 1927 the last of the reserves go. There again, had the shareholders the slightest idea that there was a sum like £232,000 excess profits duty? With the greatest respect to my friend, it is a complete fallacy, as it seems to me (my lord will direct you about it) to trouble your heads as to the date at which the money is paid. Money may be paid in any year you like, but the fact that it is paid then shows that there was a debt, only then quantified and determined perhaps; but there was a debt from an earlier period, and as a matter of accountancy and common sense the matter relates back to the earlier period. Do you think any shareholder had the slightest idea what the position in 1927 was? I put it to Lord Kysant that the newspapers, which he said he no doubt read, regarded the year 1927 as "the Royal Mail recovering." No one knows better than I do that the company was not responsible for what appeared in the newspapers, but, on the other hand, when Lord Kysant was making his speech a fortnight later, what a chance he had of correcting any false impression! Do you think that any shareholder at that meeting had the slightest idea of what was going on? Do you suppose that in the year before, when the shareholders were told that it was justifiable to transfer £150,000 from reserves, they had the slightest idea that double and treble the sum of £150,000 was being transferred from what I do not hesitate at this moment to call hidden reserves? It is not a question whether Lord Kysant thought, or did not think, that the cycle was coming again. He is perfectly entitled to his own view about cycles, but he is not a prophet, as he is careful to tell you and, just as he is entitled to his own view, so the ordinary shareholder is entitled to his own view. I submit to you as a proposition of common sense, and as being fundamental to confidence in this City, that if the business has got into this sort of position, and if the company is obviously

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in grave difficulties, it is really not for any chairman or for any director to say to himself: "Well, I am not going to tell my shareholders, because I think there is going to be a cycle and that everything is going to get all right again, and between 1928 and 1929 I am going to be in the position to pay the debt which I shall then owe to the Treasury."

Now you have to consider the use of the words "adjustment of taxation reserves," and here, as it seems to me, and I submit it for your good consideration, wholly different considerations arise between these two defendants. You know it is quite one thing to go through the process of what I may call stocktaking of your reserves—seeing whether your reserves are sufficient or insufficient, or more than adequate, to meet the contingencies against which they are provided, and to arrive at a conclusion from that point of view. The attitude of the man who approaches the subject from this point of view, namely, "I am going to find enough to meet the deficiency; where can I find it?" is not the attitude of a man who is adjusting taxation reserves at all. It simply is not adjustment. Let the adjustment of taxation reserves be taken at its face value, and let us assume that an ordinary shareholder would know what was meant. So far as Mr. Morland is concerned, it was my duty to make it quite plain to you, through his cross-examination, that Mr. Morland knew none of those things. When Mr. Morland comes on the scene the account has been prepared and approved by the directors and passed by the directors. He does not know its antecedents. He does not know that the £350,000 has been moved up to £550,000 because this Nelson bonus did not materialise. Neither does he know that Lord Kysant had started the ball rolling by asking Mr. Cason in October, 1926: "What reserves have we got available to meet the deficiency?" That is a point which differentiates their positions. Mr. Morland has said to you that he selected those words: "Adjustment of taxation reserves" because he thought they would convey a definite and precise meaning, which he said he wanted to do, to the ordinary man in the street. As ordinary men and women in the street, I submit to you quite confidently they convey no such meaning at all. It has often been said that the greatest professors in Greek and Latin languages are the worst teachers, because they cannot realise the difficulties of their pupils, and it is a consideration which, I think, you ought to take into your minds, if I may venture to say so, as to whether the possible view of this is that Mr. Morland was a little too much enwrapped in the mysteries of accountancy or higher mathematics and never descended to the plane which the ordinary common or garden man, if you do not mind being called such, occupies. It is fair to say that Mr. Morland had no knowledge of the subsidiaries; he knew nothing about them, and you have seen enough to tell you that the position of the subsidiaries certainly made this whole situation far more serious than it otherwise would have been.

Finally, it is my duty to point out to you, in order that you may give it just such attention as you think proper, that there is this vitally important distinction between the two of them: that when

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these words were used in the year 1925 and again in the year 1926 and again in the year 1927, Mr. Morland in the ordinary course of events would not read the papers or concern himself about quotations or read the accounts of the meetings or, indeed, know anything about those things. Of course he does not realise, or he may not realise, that those words have been misunderstood. But what about Lord Kylsant? You must ask yourselves, weighing the whole matter up, and bearing in mind that it is your duty to give him the benefit of the doubt, if you can, this question: supposing Lord Kylsant in the year 1925, when those words were first used, thought they were an adequate indication, did he still think so in 1926; and if he thought so in 1926, is it possible for you to remain of the opinion that he still believed it in the year 1927? If not, you get a very different set of circumstances by which to judge the two cases. But when I have pointed out to you all those relevant circumstances, I would remind you again (it is right that you should bear it in mind) that in this case you cannot convict either of these defendants unless you are satisfied that not only was the document false, but that there was a deliberate intention to put forward a false document. I cannot help regretting—a regret which perhaps many of you will share—that Mr. Morland with regard to this company, the Royal Mail Steam Packet Company, did not think it right and proper at some stage to make the same sort of statement that he did with regard to the Royal Mail Meat Transports, which you remember. I dissent entirely from the evidence which I understood Mr. Morgan to give; I dissent entirely and emphatically from the view that an auditor is not concerned with the form of the profit and loss account. He is concerned for this very simple reason: unless he is satisfied that the profit and loss account and the balance sheet and every other document fairly and truly put before the shareholders what the state of the company is, he ought not to sign it. He is there as the protector of the shareholders; he is their watch-dog, and he must try to put himself in the position and in the place of the ordinary common or garden shareholder and not busy himself or concern himself with technical phrases. To say that now does not alter the fact that, so far as Mr. Morland is concerned, I should be doing less than my duty if I failed to point out to you those facts which I think may make a very real difference between his case and the case of his co-defendant, Lord Kylsant. For reasons I have already indicated to you, I submit you must consider those two cases from rather a different angle. You have no right with regard to Lord Kylsant to find him guilty because you think his conduct was deplorable or dishonest, because you think he was prepared to gamble with other people's money, whatever hard things you may think about him. You have no right to convict him unless you are satisfied that he put forward these documents knowing them to be false, with the intention that they should deceive the shareholders. Having said that, it is my duty to submit to you in this case that those documents were absolutely false, that they obviously concealed from the shareholders the true position of the company, and that they were intended to conceal the

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true position of the company I do not doubt for a moment that it may well be true that Lord Kylsant hoped that better times would come; that the company somehow or other would get round its difficulties and perhaps get an extension of its trade facilities without its difficulties being brought to light; he hoped for something to turn up. But, whilst hoping for something to turn up, whilst trusting that things would get better, he was keeping, in my submission to you, facts back from the shareholders which made the documents he was putting forward false and untrue documents. That is the position on that part of the case, and my lord will tell you what facts you ought to take into consideration; but, I remind you again, the prosecution must discharge the onus of proof. If you are left in doubt, it is your duty to return a verdict of not guilty; it is your duty to bear in mind the wholly different circumstances which relate to the two cases, the circumstances which bear directly upon the intention, but if, on the other hand, having regard to all those circumstances, you feel that there is only one verdict here possible, do not flinch from your duty. Remember that you are performing a useful citizens' service if you are helping, in this Court, to clear up an unsatisfactory state of affairs which, in the interests of this great City, perhaps ought to be cleared up at the earliest possible moment.

Now there is one part of the case left, and I can deal with it shortly. From some points of view it is a much simpler case than the other. So far as the defendant Lord Kylsant is concerned, I think you will probably take the view that it is at least as serious and probably more serious. I or anybody in my position must always remember that a man in Lord Kylsant's position, particularly if his concern has failed, is liable to be criticised in the light of after events, and people with the knowledge of after events are only too apt to turn round and seek to find some criminality. Well, I certainly do not want to do that. It is fair on this issue that Lord Kylsant should be judged not in the light of the knowledge which you and I have to-day, but in the light of the knowledge which existed at that time. Great though his position in the City of London has been, I do not believe that any one of my colleagues who has ever held my office would for a moment differ from me in this: that if we are going to insist upon financial purity in the City of London with regard to these prospectuses or anything else, we must not merely pursue the comparatively humble share-pusher, we must be prepared to strike at the man in a big position, if he has done anything he should not have done. But because he is in a big position and has been unfortunate in his concern, that is no reason why you should condemn him. Even assuming that the debenture holders are all going ultimately to get 20s. in the £, it does not bear upon the point. If in fact by reason of untrue statements the security they were offered is far more than the security they ever obtained, the fact that they do get paid is not an answer.

Take another point which my friend laid stress on. He said: "Are you going to punish Lord Kylsant, to find him guilty, by reason of the fact that he made an error in judgment? He thought the company



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was in the trough of the wave, and was about to rise; he thought things were going to get better. He may have been right or he may have been wrong, but that was his view. Are you going to punish him for that?" As I have told you, Lord Kylsant is perfectly entitled to that view, but when he issues a prospectus to the public, the public are entitled to form their own judgment, and they are entitled to have such facts put before them as will enable each one of them to make up his own mind as to whether the investment is a good one or a bad one. It is an utterly wrong conception to think that anybody can colour a prospectus or leave out material facts, and then say: "Well, I thought that everything was going to be all right, and really if you convict me you will be finding me guilty because I made an error in prophesying." Prophecy is out of place in a prospectus. What you want in a prospectus are facts, facts relating to the present situation, from which the investors can for themselves draw conclusions as to what is going to happen in the future. No one expressed that more plainly than Lord Kylsant himself when I asked him the question. "Do you think that the duty of a person who puts forward a prospectus is to put forward all relevant facts fairly and squarely, so as to enable an investor to form his own judgment?" He answered. "Yes." I accept that test, and you all know that test is right. Well, what then is the relevance in the prospectus of stating the past? You state it in heavy type. Why? Again let me go to Lord Kylsant. I asked him this question: "Q. I am not talking about prophesying. I am asking you this. Did you intend an investor to be guided in his judgment by this consideration: 'This is what the company has done in the past and therefore presumably it will continue in the future'?"—A. It tells you what it has done in the past and it gives you an idea of what it may do in the future. Q. Exactly; and the only interest of the past to the investor under those circumstances is in so far as the past may form some indication with regard to the future?"—A. Yes." There we get from Lord Kylsant the elementary proposition that you have to state facts to enable an investor to form his own judgment; and, secondly, that the relevance of the past is in so far as, and only in so far as, it enables him to form a judgment in regard to the future. If you get as far as that, you at once realise this: if you take an average you must be very careful to see that there is nothing in that average which vitiates or falsifies the conclusion which you obviously intend the investor to draw as to the future. You will remember the ten years' average started with 1918 and ended with 1927, and when I put it to Lord Kylsant he agreed that the situation which prevailed in 1924 was wholly different from that which prevailed immediately after the war. My friend put before you the case of a cricketer, and he said: If a cricketer comes and seeks an engagement and he says, "My average is 50," is it really material that he obtained most of his runs in the early part and has rather gone off colour in the later part of the season? Of course not. He states an average, and that is a perfectly fair thing to do. Let me take this perfectly simple case. Take a cricketer who had an average of 50 in one year, and in the off season,

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while out rabbit-shooting, he gets a pellet in the right eye and loses the right eye, and then, minus an eye, seeks an engagement in the following year and says: "I played all through last year and my average was 50," but says nothing about his right eye. Is it not perfectly obvious to anybody outside a nursery that that man is being fraudulent? Why? Because it is fallacious and dishonest to base yourself upon an average, if in fact there has been a complete change in circumstances which renders that average an untrue criterion of the future. Where you take the cricketer with his average, he being sound in wind and limb, and so on, what he gains in the early part of the year he loses in the latter part of the year, and that is perfectly right. But if you take a case like this, where you are dealing with a situation in 1918, 1919, and 1920, which is wholly different from the situation as it exists in later years, do you think it was honest? My friend says: "Oh, but are you to regard all these investors as babies?" Members of the jury, these prospectuses do not go out only to people in the City of London—they go up and down all over the country. I daresay there is many a country parson and many a country schoolmaster who receives this sort of thing. Do you think it is an honest thing to put forward a statement of this sort and then, when it is criticised, get some distinguished counsel to say that you must not treat these investors as though they were all babies? No. In my submission to you, this part of the case admits—no, necessitates—an answer which is far easier to arrive at than the answer on any other part of this case, and, if proof were needed of that, just let us see what Mr. Morland said when I asked him about writing back. I asked this question: "The object of the alteration, or writing back, would have been for this purpose, would not it, to avoid a member of the investing public being misled?—A. If you put it in that way; I should put it to give the necessary information to enable him to form an opinion." Now, observe that.

The test is not whether there are 14 million of unsecured assets; it is not whether the investors would ultimately get paid in full; the test is the answer to this simple question which I put time and again: Supposing the true facts as we now know them had been set out, is there any one of you in that jury box who would have had a shadow of a doubt that there would have been no subscriptions whatever for an issue which was going to give something less than, I think, 5 per cent.? I asked Lord Kylsant the question: "If the figures were set out in the prospectus as they are on this statement, have you any doubt that not one single investor would have invested?—A. I would not let any incorrect figures be set out in any prospectus with my name on it." I try again. Q. I want to get your answer to the question. If these figures were set out in the prospectus as they are on this statement, it is manifest, is not it, that nobody would have invested in this?—A. If you publish a misleading statement about anything, you would not get any subscriptions." I try again. "Q. Let us try again. Apply your mind to my question. If the facts had been set out in the prospectus as they are on this statement, would anybody have subscribed

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to this? " and then he says: " The answer to that is, if they were set out as they have been proved in this Court to be, there would have been a good response to the issue." You can judge of the truth or falsity of that answer without any further observations from me. You know what the results of the trading in the years 1921 to 1927 had been, and you can imagine how this statement would look if Mr. Morland had set out year by year what had been done. If Mr. Morland had been asked he would have insisted upon doing that to enable, as he said, an investor to form his own opinion. Just think, leaving out the question of average for a moment, and ask yourselves as men and women of common sense if there is a shadow of doubt if this had been set out in this way that there would have been no subscriptions, and still less no over-subscription. We cannot be too careful to insist upon scrupulous honesty in the prospectuses which go forth. It is so easy for a clever person to put forward a document with regard to which it is possible to say every single sentence is true, and yet the document is wholly false. You must consider whether Lord Kylsant, when he put forward these statements, did not do so with a view to deceive those who might entrust money to the company. It is not a case of whether you think that the document is tricky, or too clever, or dishonest; that does not entitle you, whatever you may think, to find him guilty; you have got to find that this document, taken as a whole, is false, and was intended to be false, and was intended to deceive people who were going to invest money in this company.

The only other point on the prospectus I want to deal with is this. You may think that of all the deplorable statements the truth of that statement about adding to reserves is one of the worst. The attitude of mind of a man who can say under those circumstances, " I have in the year 1924 added to reserves " when he has taken out of the unpublished reserves far more than he has added to the published reserves, is one which I do not think needs further comment.

Members of the jury, I have finished in what I may say I think has been for me the most anxious and the most worrying case I have ever had since I have been at the Bar. I have tried with all my ability to do everything I ought to do to arrest a certain laxity which I think I perceived in this case, a laxity which does not redound to the credit of this country, a laxity which if it continued might prevent a restoration of confidence among our people. The overriding consideration for me and my learned friends is this: that there shall be no danger that any innocent man shall be convicted merely because you disapprove of his conduct or dislike his methods. If, on the other hand, you feel that this case is brought home, do not hesitate to do your duty because you have heard about anxious nights or warders and chains, or anything of that sort. You will serve your country best by doing your simple, plain duty.

Having addressed you in this case, I hope at not too great length, I submit to you with regard to this last matter which I have been discussing, the question of this prospectus, there can be no reasonable doubt in your mind but that it was, taken as a whole, a dishonest

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document, a false document, put forward with an intention to deceive investors, and it did deceive them.

I submit with regard to Lord Kysant that on the other two charges, with regard to 1926 and 1927, you ought equally to find that those accounts were false, that they did not give to the shareholders the information the shareholders ought to have had, but, on the other hand, they conveyed a wholly untrue picture of the position of the company. I submit you ought to find that those accounts were put forward to prevent the shareholders knowing what the true position was in the hope that it would turn out to be all right.

With regard to Mr. Morland, I have thought it my duty to point out to you certain facts which in my opinion sharply and clearly differentiate his case from the case of Lord Kysant. The question I suggest for your consideration is as to whether this phrase, a phrase used by an accountant, perhaps too readily used by an accountant, was used under the impression that it would convey to other people the meaning it would convey to him, or as to whether you think he meant to deceive. If so, then in his case, too, it would be your duty to find a verdict of guilty against him. It is right that you should always remember in Mr. Morland's case he had no motive whatever for being dishonest so far as his financial position was concerned, and, therefore, you will probably be slow to take a view which is hostile to him merely because you think he used a phrase which ought not to be used, if he had determined to do what he says ought to have been done to bring this matter home, to put it plainly, and to put it beyond peradventure before the ordinary shareholders, whose concern, after all, was his.

Members of the jury, I have done. You will have the benefit of an examination of the figures by my lord, and the view of the law from my lord, who will be able to assist you more than any of us has done, and with that I leave this matter in your hands, knowing that under my lord's guidance you will play your part as citizens and give a true verdict.

Adjourned.

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Ninth Day—Thursday, 30th July, 1931.

## Charge to the Jury.

MR. JUSTICE WRIGHT—Members of the jury, you have sat for several days listening to this case, and the time will soon come when your voice will have to be heard, and heard at a decisive and crucial moment. Between that moment and now there is my summing-up. As you know, it is the duty of a judge at the end of a criminal trial to sum up to the jury. It is his duty to tell them to the best of his knowledge and understanding what is the law which they must apply to the case in hand. It is also his duty to analyse the evidence which has been given, by way of reminding them, and putting things together as well as he can at the end of the case, and in that way to lead the jury to do what is their duty, and their duty alone, in arriving at a decision on the case. While a judge can only, as you may imagine, do his best to be accurate in his epitome of the facts, he may well fall into error in his statement of the facts, and he may also err, according to your judgment, in omitting things or in stating things which are, in your opinion, not very material, or in over emphasis or under emphasis. While you take the law from the judge, because that is his responsibility, the summing-up as regards the facts, which the judge addresses to you, does not in any way bind you. You are the judges of the facts. You have heard the evidence from the beginning to the end, and I need not say you have listened to it with the greatest care and attention, through this very long and trying case. You are the judges of the facts, and it is on you that the burden and responsibility must rest.

I have said that this is a trying case, but it is an important case, because it has involved the ventilation in the City of London and in this Court of many questions connected with the finances and accounts of companies—a matter of the very highest public importance. I am bound to say, and I say it because of things which have fallen from time to time quite properly and not unnaturally from various speakers in this case, that, quite apart from any question of success or failure, I think that the prosecution in this case has been, and will be, of very great service to the commercial community. The position here is that you have to consider whether these sections of the criminal law which are enacted for the protection of shareholders in joint-stock concerns have or have not been infringed. The Crown, in considering the question of the prosecution, have only to act according to the best of their skill and judgment in what appears to them to be a *prima facie* case. That is their function and their duty; and it is their further duty, when the case comes on for hearing, to present the facts as they understand them fairly and temperately to the jury, but the eventual result of the trial must depend on the decision of the jury when they have heard

# Charge to the Jury.

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all the facts and all the evidence. That is their function. Now, that being so, what is the position here?

Before I deal with the sections, and before I deal with the actual charge which you will have to consider—and that is the essential part of the case—I want by way of warning and distinction to point out that you are not here concerned with several other matters which have incidentally arisen, or at least suggested themselves, in the course of this inquiry—questions, I mean, as to what is the general law as to the keeping of accounts; questions as to what are the general duties of auditors; and questions as to what are the true functions and true contents of balance sheets and profit and loss accounts. These are important questions of very great public interest, and no doubt everything that has happened in this case will be of value to those whose duty it is to see that the law on these matters is observed, and if it is unsatisfactory or insufficient for the purposes for which it is intended, to take steps to have it improved.

A great deal has been said about the keeping of secret reserves, and how far that is or is not permissible under the Companies Acts or under the special charter of the Royal Mail Steam Packet Company, because, as you will remember, the questions which arise here fall to be decided, so far as that aspect of the matter is for your decision or your consideration at all, under the special charter of that company. We have heard a great deal about the keeping of secret reserves, and we have heard a great deal about the commercial troubles which may flow from that practice. We have heard a great deal about what is often done in practice, and it may be reasonably and properly done, but the question may arise some day, and possibly will arise, in some appropriate proceeding in order to find out and elucidate these very special matters. It was said by a very learned judge on one occasion, by way of observation and not by judgment, that a company, that is to say the shareholders, could not complain if the position of the finances of the company was better than the accounts disclosed. That has been quoted from time to time as a justification for this method of keeping reserves secret. But there may be very great evils if those who have the control and management of the companies, and who control and manage companies for the benefit of the shareholders who entrust their moneys to companies, have very large portions of the company's assets left in the secret disposition of the managing authority. It may work very well in many cases; no doubt it does. It is a practice which is being followed, no doubt, by many concerns of the highest standing. On the other hand, it may be the subject of almost intolerable abuse. Such a system may be used to cover up negligences, irregularities, and almost breaches of faith. It is said to be a matter of domestic concern between the company and the shareholders, but if shareholders do not know and cannot know what the position is, how can they form any view about it at all? How can they consider whether it is something which they are satisfied with or which they are not satisfied with? Taking this case, without entering into the thorny question as to whether you have here anything which

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can be called reserves or not, you have here a large sum of money, or perhaps a series of large sums of money, the nature of which and the propriety of which has remained a secret from the shareholders, and the use of which has remained a secret from the shareholders, if you exclude certain things which appeared in the three last balance sheets with which we are concerned. What has happened as a result of that? We know that there were balance sheets and profit and loss accounts published for a period of seven years which did not disclose one way or the other whether the company was earning any profit or not, and during those seven years there was expended out of those items, which were mainly connected with the war, a sum of no less than five million pounds—not out of current earnings at all, but out of these items which in the main, arose out of the war; and during all that period the shareholders were told nothing, and they drew their dividends presumably in the simple faith that all was well with the condition of the company. It is said: “Very well, they got their dividends. Times might have changed, and although these items of income came to an end others might have taken their place and conditions might have improved.” But, on the other hand, surely if the shareholders had been told (I do not say who is responsible for the moment) that this company had no earnings—because earnings are the life blood of a company, and a company cannot go on indefinitely using its capital assets unless it is earning—if they had been told that this company had no earnings, surely they might have taken steps, as could be done, and as has been done in other cases, for the reconstruction and rearrangement of the company’s affairs, the cutting down of expenditure, the reduction of services, and all those things which have to be done when a company is not paying its way. The sooner that is done the better, and the better hope there is of the company surviving the troublous times. I will say something about what appeared on the profit and loss account a little later. It was never brought to the shareholders’ knowledge what the position was. It may seem incredible that this could go on in a big company for all those years, but so it was, and then eventually at a period, which is outside the period we are concerned with, something had to be done and some steps had to be taken. It is a little astounding, and one cannot help wondering whether those who manage big companies do not forget sometimes that the body of directors of a company are the agents and the trustees of the shareholders, that they owe them full information, subject to proper and reasonable commercial necessity, and it is their interests that they have to study. They are not to regard shareholders as sheep, who may look up if they are not fed; they are the people whose money they are using, and it is to be remembered that a joint-stock company is a creation of law. A joint-stock company has the enormous advantage of limited liability, and the legislature has intended, it seems to me, although by halting steps, to secure that those who enjoy those privileges of limited liability and who control and manage joint-stock companies should be subject to some condition as to publishing their accounts,

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at least to the shareholders and at least to those who are entitled to be summoned to general meetings.

The law has recently been altered in the Act of 1929, and for the first time that has provided for the sending to shareholders of a balance sheet, and a profit and loss account in every year; and there are penalties imposed upon directors who do not do that. The balance sheet must contain a summary, among other things, of the liabilities and assets together with such particulars as are necessary to disclose the general nature of the liabilities and assets of the company, and to distinguish between the amounts respectively of the fixed assets and the floating assets, and state how the values of the fixed assets have been arrived at. It further provides that there is to be a report by the directors with respect to the state of the company's affairs, and the amount, if any, which they propose to carry to the reserve fund, or any other reserve. It may be said that that does not in terms prohibit the creation of any reserve which is not shown specifically on the balance sheet, and it may be said that in a matter of domestic concern like the keeping of reserves by appropriate regulations the shareholders may agree to a reserve being accumulated, the exact amount of which is not specified in the balance sheet or the profit and loss account. That is a question which, no doubt, will require very careful consideration in some future case, but it does appear to me, as at present advised, that the terms of the sections which I have read cannot possibly justify the omission of any amount of any reserve from the balance sheet and the profit and loss account altogether. There may be some justification for the maintenance of an undisclosed or secret reserve, if the fact that there was such a reserve was clearly specified somewhere in the report, so that the shareholders could know, and if the majority of them desired to insist on its disclosure and its amount and its utilisation they could do so. However that may be, it is clearly the intention of these sections that the accounts of companies in future should be published with greater particularity and with greater information to the shareholders.

Then there is the question of the auditor, because, as you will remember, the law requires the appointment of an auditor, who is the servant of the company, and his duty is to report to the shareholders, on proper examination, on the accounts which the directors are going to present to the company. The law does not impose an impossible burden on auditors; it does not make them insurers; it does not require of them skill and vigilance which is beyond their power; but it does require them to report, and to report on the accounts would certainly include a very careful investigation of the profit and loss account as one of the accounts, even if it is not expressly covered in the certificate which is generally accepted as a complete report. Then they have to give a certificate as to whether in their opinion the balance sheet referred to in the report is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs according to the best of their information and the explanations given to them. Now, if the account on which the dividends are being paid, or if the account on which the current expenses of the company are being met, is being fed



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by undisclosed reserves, it seems to me very difficult to see how the auditor can discharge his duty of giving a true and correct view of the state of the company's affairs without mentioning and drawing attention to this fact, which may be of the most vital importance, as indicating the state of the company's affairs. No doubt an auditor, in his very delicate and difficult duties, must use a certain amount of discretion, but, whatever discretion he may feel that he is justified in exercising within the limits of what is reasonable, he must remember that he is under a statutory duty, and that he may come under the penalties of the law if he fails in that duty, at least in specific ways which I need not trouble about at this moment.

That is the position under the new Companies Act. It is rather more stringent than the position before 1929, but in this case you will remember that we are dealing not with a company under the Limited Liability Companies Act to which those Acts apply, but we are dealing with a company which is formed as a corporation and which has the privilege of limited liability, and that corporation is governed by the terms of the charter which is granted to it by the Crown, because it is the Crown which grants the charter which incorporates a chartered company. There are very few chartered companies. It was a practice which was followed in the earlier days before the system of the Companies Acts had been invented and developed, and in those days a corporation could only be created by the special Act of the Crown or Parliament. I do not remember which was the last chartered company which was formed, but this company, one of the very oldest shipping companies in this country, was formed in September, 1839, and, as you know, there are certain provisions which deal with the keeping of accounts. So far as I have been able to ascertain, and the learned counsel agree, the words which I am now going to read are the only words which deal with the accounts which the court of directors have to lay before the general meeting. They are as follows:—"Previously to every yearly general meeting an account shall be prepared by the court of directors of the debts and assets of the said corporation with an account of the profits made in the year ending 31st December preceding such general meeting for the time being, as near as the same can be ascertained, and with all such information as may to the directors seem necessary to be given or as may be required by any bye-laws of the corporation, which accounts shall be signed by at least one of the directors of the corporation and shall be laid before such meeting to be audited and settled as aforesaid." Now, that remains as an obligation on the court of directors to prepare and lay before the meeting each year an account of the debts and assets of the said corporation, and an account of the profit made in the year. Then there are certain provisions in a later charter as to having reserves, and there are certain provisions as to the auditors altering the position which was established in the original charter, because in 1904, that is to say after the Act of 1900 which made the appointment of auditors obligatory on companies under the Companies Act, there was this section in the supplementary charter of that date: "We do further will and direct that so much of the

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original charter as requires the auditor of the company to be the holder of stock in the company is hereby rescinded." That is, I suppose, because in the old days the auditor was not a professional auditor; he was probably a member of the company who looked after the accounts. Then it goes on: "Notwithstanding anything in the said original charter contained to the contrary, the following provisions as to auditors and audits are to have effect." That does not alter in any way the provision requiring directors to give an account of the profits, but it deals with the position of the auditors, and it is a reproduction, I think, word for word, although I have not compared it verbatim, with the provisions of the Companies Act, 1900, which still remain in the Companies Act of 1929. It provides that the auditor shall have the right of inspecting the books, and so on, and that he is to sign a certificate stating whether his requirements have been complied with, that he is to make a report on the accounts; and he is to state in that report whether in his opinion the balance sheet is properly drawn up so as to exhibit a true and correct view of the state of the company's affairs as shown in the books of the company. As you all know, a balance sheet or profit and loss account does not condescend to detail, it is not a trading account, but one would think that it must at least show that essential element which seems to be the reason why you want a profit and loss account. A profit and loss account which conveys no information to the shareholders would be of little use. An auditor is not concerned with questions of policy, and it is not for him to say whether a dividend is properly or improperly declared, but, if he sees on the accounts there is something in the accounts to which he ought to draw the attention of the shareholders, it is his duty to do so, and either he should not sign the certificate at all or he should sign it with some qualification such as the circumstances require. There is only one clause, so far as I know, in the supplementary charter, or any of the charters, which deals with the power of the court of directors to keep a reserve: "The directors may before recommending any dividend set aside out of the profits of the company such sums as they may from time to time think proper, as reserves, insurance, or suspense funds. All sums so set aside shall at the discretion of the directors be applicable for meeting any losses, contingencies, or any depreciation in any of the company's assets, or for the gradual liquidation of any debt or liability of the company, or for repairing, renewing, or maintaining any property of the company, or for equalising dividends, or for distribution by way of dividend or bonus among the members of the company in accordance with their rights, or for any other purpose which the directors in their discretion may deem to be for the advantage of the company. Provided that only such parts of any reserves or other fund as shall from time to time in the opinion of the directors represent undivided profits properly available for dividend shall be distributed by way of dividend or bonus." So far as I know, in the charter there is no provision for the maintenance or for the creation of a secret reserve fund. There may be, but it has not been pointed out to me, and I have not been able to discover it.

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That being the state of things, the question to be decided by you in this case is not whether the two defendants, or either of them, have committed any breach of their duty to the company, either as chairman or as auditor. If there has been any breach of duty, not negligence, but anything for which the directors or the auditor may be liable to the company, that is a matter entirely beyond your purview or beyond your consideration. You are not here dealing with questions of civil liability. For civil liability the appropriate remedy is an action for damages; but when a matter comes before this Court it comes as a matter of criminal liability; it comes before this Court because there has been some infringement of the law which goes beyond the purview of civil liability, which is merely answered in damages, and which amounts to a crime against the State, of which the State must take cognisance, and a crime for which the party who is convicted must receive a sentence appropriate to a criminal.

There is only one other general observation I think it may be convenient for me to make before I deal with the indictment in this case, and that is this. that it is a universal rule of English criminal justice that every man who appears in the dock on a criminal charge is in the eyes of the law innocent until he is proved to be guilty, and a jury cannot convict a man of any criminal charge unless they are satisfied beyond reasonable doubt that he is guilty of the offence charged against him. One sometimes hears it said in a criminal case—I have heard it said—that questions of public policy, questions of public morality, questions, it may be, of financial purity, are involved, and things of that sort are stated to the jury. I do not think anything of that sort has been said in this case. It may well be a very strong and urgent ground for the Crown, in deciding whether to launch a prosecution or not, to consider whether the matters which appear to them to call for investigation are matters which affect the public interest, or matters of financial purity, but this is not a consideration which can weigh with a jury in arriving at their decision. It is either illegitimate or unnecessary. They have to decide on the facts and on the evidence in the special case, and therefore these considerations which I have adverted to are illegitimate if the evidence is not strong enough of itself to justify a conviction, and unnecessary if the facts are strong enough. Therefore, what you have to do is simply to decide according to the definition of the offence, which you must take from me, and according to your view of the evidence, which is a matter between you and your conscience, and with which no one else has any right to interfere.

The indictment charges Lord Kylsant with circulating a false statement with intent to deceive shareholders. So that the only relevant intent here is an intent to deceive shareholders. If you thought that there was an intent to deceive some one else you would ignore that intent, because it would be outside the scope of the indictment. The relevant intent is an intent to deceive shareholders. Then it goes on in this way: "Particulars of the offence. On the 11th day of May, 1927,

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being a director of the Royal Mail Steam Packet Company, did make, circulate, or publish, or concur in making, circulating, or publishing a certain written statement of account, that is to say, an annual report of the directors of the said company, for the year 1926, dated 11th May, 1927, for the year 1926 which you knew to be false in a material particular, in that the said annual report concealed from the shareholders the true position of the company with intent to deceive the shareholders." Then Harold John Morland is charged that he aided, counselled, and procured, and so forth. What I have to say about his case I shall defer for the moment. There is a similar count, the second count, relating to the report of the board of directors for the year 1927, which is in identical terms; and then the third count charges Lord Kylsant, as being a director, with circulating a false statement with intent to induce persons to entrust or advance property to the company, and that refers to the prospectus with which you are already so familiar. That was a written statement inviting the public to subscribe to the issue of 5 per cent. debenture stock in the Royal Mail Steam Packet Company, which he knew to be false in a material particular, in that it concealed the true position of the company, with intent to induce persons to entrust or advance money to the said company. So the intent, as regards the prospectus, is a different intent, similar perhaps, but different in its application and intent; it is an intent to induce persons to entrust or advance property to the company.

Now I think it would be convenient for me to read to you section 84 of the Larceny Act, 1861, which deals with publishing fraudulent statements. It says: "Whosoever, being a director, manager, or public officer" (public officer would include the auditor) "of any body corporate or public company, shall make, circulate, or publish, or concur in making, circulating, or publishing any written statement or account which he shall know to be false in any material particular with intent to deceive or defraud any member, shareholder, or creditor of such body"—that is the first matter we are concerned with on the account. Then it goes on to say something which is not material, and then it says: "or to entrust," that is to say, with intent—"to entrust or advance any property to such body corporate, or public company, or to enter into any security for the benefit thereof, shall be guilty of a misdemeanour." That is the section. It seems to me, as Acts of Parliament go, to be reasonably clear and not to require any particular exposition, except that I want to emphasise certain aspects of it, and I want to state what is the construction I have arrived at on a point which may be important. A point has been raised or adumbrated as to the meaning of certain words. These are the words which it is said require some consideration, and I confess I think they do. It is these words: "make, circulate, publish, or concur in making, circulating, or publishing any report, statement, or account which he shall know to be false in any material particular." What exactly does that mean? The conclusion I have arrived at is this, that it is not limited to a case where you point to a written account or written statement and say:

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Here are certain figures; here are certain words which are false I think that is to narrow unduly the words "in any material particular" It is perfectly true that in a criminal act, which carries with it the penalties of the criminal law, the Act must be strictly construed, but it must be reasonably construed, and in my judgment to construe it in that way would be to shut out a type of fraud in connection with written documents or written accounts which may be of the utmost importance, and that is the type of fraud which may be found in a document, not fraudulent in the sense of what it states, but in the sense of what it conceals or omits. It may be said that you cannot put your finger on any actual statement and say it is false in a material particular, but I think the language which is used means more than that, according to its reasonable interpretation. It will cover the case where you have a written statement which is false, not in any specific words or any specific figures which it contains, but which is false in the way in which a document may be fraudulent, namely, where you may take every word and every figure, and say, "Now, there is nothing false about this; there is nothing false about that," but the document as a whole may be false, not because of what it states, but because of what it does not state, because of what it implies. Of course, that type of falsity, which is indeed the type of falsity in the main question here, is more difficult to establish than the case where you can point to a specific false word in a sentence, because where the falsity consists in a fraudulent desire to create a false impression, while keeping accurately to the limited facts which appear in the document, you have to show affirmatively that there was a deliberate intent to create a false impression. If you have a definite falsehood, that speaks for itself. A man who has told a definite falsehood or written a definite falsehood may perfectly well be able to show that, though it was false, he did not know it was false, or in certain cases, though he knew it was false, he did not intend to deceive anybody, but made a false statement, an inaccurate statement, thinking that it was substantially true, though he knew all the facts which ought to have told him it was untrue. That is a much simpler case than where you have a case in which a written statement is alleged to have been false in the sense that it was concealing the true facts. Then you have to show before you can get any further at all that it was a deliberately concocted instrument, the instrument of a definite scheme to defraud or to deceive, as the case may be, and, therefore, in order to prove a case of fraud of this latter type, fraud as it were by concealment, the intent of the parties must be established at the outset. But to construe section 84 so as to exclude from its ambit that type of fraud in a written statement of account is, in my judgment, to limit unduly the scope of the enactment, to exclude from it some of the most important types of false documents which in this class of case may have to be dealt with. The language must be construed reasonably, according to its natural meaning, and in my view, having regard to the whole of this section, its purpose and its character, I think the construction which I have given to it is the

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true construction. I have to decide this myself and you must take that view of the section from me. Of course, if I am wrong and the necessity arises hereafter, there are other Courts who can deal with the matter. My duty is to decide to the best of my judgment, and that, in my view, is the construction.

Now, as you see, the section involves three things, a false written document, knowledge of the falsity—that means the recognition, the understanding, the realisation of the falsity by the person who publishes it and puts it forward—and, thirdly, the intent to deceive. The intent to deceive is a quite separate thing. You may have the first two steps; you may have a false document, and you may have it published knowingly, and yet there may not be circumstances which justify you in finding that there was an attempt to deceive. In fact, in one of the sections of the new Act—I think it was also in one of the earlier Companies Acts—you have the offence, the misdemeanour, of publishing a false document knowing it to be false, but with no reference to the intent to deceive, which is left out, just as in some other criminal offences of a more obvious character the intent is not a necessary ingredient. But here the intent to deceive is a necessary ingredient as regards the accounts to deceive shareholders, and as regards the prospectus to deceive possible investors, if I may compendiously explain the position. The intent must be established, because if a man publishes a false statement knowingly it may be that *prima facie* he has an intent to deceive the person to whom it is published; but that is only *prima facie*, and I am not considering any question of the burden of proof here, because it seldom arises in criminal cases. But it may always be shown, and the jury are always entitled to find, that though there was a false statement published knowingly, the intent was absent, just as where you may have a case which is *prima facie* murder, but the accused man, though he did the act, might show that the relevant intent was absent. Then, of course, he cannot be found guilty of murder. If he is found guilty at all it is of some minor alternative offence which is open to the jury.

Just before I leave these general considerations I might remind you again that you are dealing with questions of criminal intent. Sir John Simon read a passage in a famous summing-up in one of the early cases under the section and, though I think I have said in effect what is stated there, it is most admirably put, and I should like to read it to you. The Chief Justice of those days said:

In a case of this kind we are, as it were, upon the very confines which separate civil and criminal law, and we must take care that we do not overstep the boundary line. It is one thing that a man may make himself liable to an action, or may be liable to have a contract which he seeks to enforce held to be vicious and bad, because he had stated something which went beyond the exact line of truth, or has concealed some material facts which ought to have been made known to the other contracting party. More than this is required to support this charge. A man may honestly misrepresent, that is to say, he may state as true something which he believes to be true, and which turns out to be untrue. If he has given a warranty, or has entered into a civil contract founded on the assumption of the fact in question, he may be liable in a civil

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action to be defeated, but that would not be sufficient for the present purpose. Here you must be satisfied that that which is alleged to have been misrepresented was known to the defendants to be false, and that, acting upon that knowledge, and with the deliberate intention to deceive and defraud, they did that which is alleged to have constituted the criminal offence for which they are now put on trial.

I think probably I have only been repeating what you have heard during the last ten days, but it is my duty to repeat it, and to repeat it with all the solemnity of which I am capable in the course of this summing-up.

I can now pass to the matters of fact which you will have to consider. I have read to you the charter. You will remember that this company in the year 1911 was a very much smaller company than it is in the period with which you are concerned. In 1911 it had ordinary and preference shares amounting to £1,700,000, debentures amounting to £2,250,000, an insurance fund which was then only £300,000, and a reserve fund which was then only £420,000. In 1921 its capital, ordinary and preference, was £6,800,000; its debentures were £4,500,000; its reserve was then £1,600,000; and its insurance fund was then £1,022,288. It appears that this company, in certain aspects of its business, followed a conservative and, indeed, an old-fashioned routine, though there can be nothing wrong in that. Automatically the insurance fund increased, first by a rate of 3 per cent. and later by a rate of 2 per cent, and that insurance fund was essentially a surplus fund. I need not trouble you with the details, because they are very clearly set out in the document. It was in effect an extra reserve. It went on increasing during the period from 1921 to 1927 automatically in the routine of the company, and it was never interfered with. During the seven years in question it increased by £300,000. The reserve fund remained at £1,600,000 from 1921 onwards, except that in 1926, as you remember, it was reduced by £150,000. Then the rate of depreciation followed year by year was a depreciation of 5 per cent., a liberal depreciation, because it may well be that 4 per cent would have been sufficient.

Now, as a matter of history, in 1929, as you have heard, a question arose about a matter of £5,000,000 which had been guaranteed by the Government under the Trade Facilities Act, and which, if I have got the dates right, fell due according to its original tenure in 1929. Lord Kylsant applied for an extension. That led to an investigation being undertaken of the company's affairs, and Sir William M'Lintock, whom you have seen, conducted that investigation and made his report in March, 1930. In the course of that investigation he was concerned, and indeed only concerned, with the ascertainment of what were the current earnings of the company during the relevant period, because the Government, I gather, before desiring to prolong the guarantee to that extent wanted to know what the company was doing, and they wanted to know what its current earnings were. Sir William M'Lintock, accordingly, with that object in mind, undertook to make an inquiry, and he made his report in March, 1930. In the course of that report he referred to some very large sums of money which had been applied

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in the affairs of the company from 1921 onwards, and referred to them as reserves. He gave evidence, and was somewhat, I will not say rudely, but somewhat crossly examined about the use of this word "reserves," and he not unnaturally retorted that he had only taken the word because it was a word used by the company's officials themselves; and indeed everybody seems to have called them reserves until some date in the course of this inquiry. It may be there was a reason for calling them reserves, because if they were reserves they were undistributed income, and if they were undistributed income they could be used for paying dividends. But I know nothing about that. All I want to point out is this. I am referring to Sir William M'Lintock and his most valuable evidence, who conducted his specific inquiry, every one agrees, with the most precise accuracy. There is only one figure criticised, and some observations about depreciation in 1926 which I think are material. He pursued his investigations, as you would expect from a man of his eminence in a distinguished profession, with complete accuracy, and he made his report. I must say I thought he gave his evidence with absolute fairness and with a studied accuracy and moderation. I do not know why I should say moderation, because he had no reason for anything else; he was not concerned in the matter at all. It was the material which he obtained which, as I understand, drew the attention of the authorities to what had been happening in this company.

The period in question which you have to consider is from 1921 to 1927, or more specifically you have to consider the two years 1926 and 1927, when you are considering the accounts, because it is to those two years that the specific counts in the indictment refer. I have already said that you are not concerned with any question of civil duty as between the company and the two defendants, or either of them. In saying that, may I remind you of what the case actually is which is put forward by the Crown? For this purpose they do not lay any stress on the precise rules of law as to the completeness of a company's accounts, or the accounts of this company, or the precise duties of an accountant. What they say is: Assume that, as the practice is said to be general, the directors may be justified in putting money to undisclosed or secret reserves. Assume that they may use these secret reserves without telling the shareholders for some period of time, and do that properly. Assume all that, yet a time must come when, if that is done to a large extent, with large sums of money, or if it is done over a long period of time, you have then a circumstance so vitally affecting the life of the company, and vitally affecting the interests of the shareholders, that any deliberate concealment of those circumstances is a breach of duty on the part of the directors or auditors, and, if done fraudulently, with intent to deceive, constitutes an offence against the State. I do not gather now that there is any real question as to the general accuracy of the view that a very heavy, or a very long, protracted utilisation of secret reserves, in order to keep the company going, is a serious matter which, quite apart from anything I have said about the



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general law, ought to be disclosed, on any view of the position, to the company. I made a note of how that matter stood on the evidence.

You have had the benefit of hearing the evidence of that very distinguished accountant, Lord Plender. There was a question put by Sir Patrick Hastings. Lord Plender is a little guarded in what he said. He was asked: "Q. There are such cases, that is to say, cases where there is no longer a requirement to keep a reserve for excess profits duty, that is introduced into the credit of the year's profit and loss, and no mention is made on that occasion that reserves have been called upon?" Lord Plender said. "There are such cases." Then I put a question: "Q. You mean that has been done?—A. It has been done" "Q. So far you express no view about it?—A. It is done by firms of the very highest repute" Then he is asked if any exception could be taken to that, and he says: "As a principle no exception could be taken." He was definitely guarded. Then he was asked: "Q. There would come a time when the auditor would say 'Now, if these reserves are to be used again, some indication must be given to the shareholders that the profit and loss account is augmented by transfers from the excess profits duty or other reserves'?"—A. Yes."

Then there is a question as to what phrase is the proper one to use. There is a phrase, which may be very familiar to you, but as far as I know is not suggested as being familiar to anybody but accountants. I do not know how that may be. There is the question whether the addition of those words in the balance sheet in the year 1926, "Adjustment of taxation reserves," was, in all the circumstances of the case, a proper method of illuminating the minds of the shareholders as to what was actually happening. That is a question which you will have to consider and on which you will have to give a decision one way or the other. Is this phrase "Adjustment of taxation reserves" a proper intimation to the shareholders in 1926 of what has been going on in the company's affairs, in order to produce year by year not only the debenture interest and the interest, discounts, and other things, but the preference dividends and the ordinary dividends? I am going to say a word about the facts in a moment, but at present I am reminding you—although I am sure you have it all present to your mind—of what appears to me to be the first question you have to consider. Granted all this, was it false and misleading in all the circumstances to put forward to the shareholders in the balance sheets in those years merely these words "adjustment of taxation reserves" as a warning that these enormous sums were being drawn from these funds, the nature of which I must consider a little later?

Then, as to those words, Lord Plender gave his definition—and I might remind you of it perhaps, though I expect you remember it. I asked him to put those words into plain English. He said he had been thinking it over during the night, and then he said: "The definition I would give to it is this: The difference between a sum or sums reserved or set aside to meet maturing obligations, whose precise ascertainment is not known at the time such provisions are being made,

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and the amount of the actual liability when it is ascertained and settled."

Lord Kysant was asked about this matter. Perhaps before I turn to his evidence I may refer to the evidence of Mr. Hill. He was asked in cross-examination. "Q. You agree with me from the accountants' point of view this matter is a matter of degree?—A. Exactly" That is the matter of transferring sums from reserves without disclosing them. Then he was asked: "Q. Whether you are right or wrong in law, we are not debating in this case, because, as I say, this is not the proper arena, but in fact transfers from a reserve fund are sometimes brought into profit and loss account without any notification of it at all?—A. That is so. Q. Then there comes a stage whether, as Mr. Morland said, it reached a matter of time or by the size of the amount—there comes a stage when some indication must be given?—A. Yes, some indication. Q. Some indication. Does there finally come a stage when there must not merely be an indication, but a perfectly precise phraseology when nobody can make a mistake about it?—A. I should think so. It depends on the circumstances; one cannot generalise exactly" So that Mr. Hill, the president of the Institute of Chartered Accountants, says there does come a stage when some indication must be given, and he would think there came a stage when a perfectly precise phraseology that nobody could mistake ought to be used, though he does not want to generalise.

Then Lord Kysant was cross-examined on this point. I do not want to weary you, but I think I ought to read what he says about it. I only want to pick out a certain number of passages. If I am leaving anything out which is material—a risk one always runs when one selects—I would be thankful for any intervention.

Sir PATRICK HASTINGS—I am sure I may ask your lordship to read one question in Mr. Hill's evidence where he said that the phrase used was a proper one.

Mr. JUSTICE WRIGHT—Yes. He says: "I think it is quite suitable."

Then Lord Kysant is asked: "Q. In this your understanding, that if you have an exceptional loss of a temporary character, if you call attention to that you might, so far from reproducing a true and accurate view of the company's position, give a false impression of the company's position?—A. Yes, I agree. Q. However good the principle may be, nearly all principles can be misapplied, can they not? I will put the question in this way: Would you agree that the extended and continuous utilisation of large sums drawn from secret reserves without any indication at length becomes misleading?—A. It certainly could under certain circumstances."

Then the question put to Lord Plender is repeated, and is put: "Q. You would agree that there does come a time, to borrow his phrase, when some indication must be given?—A. There might come a time, certainly. Q. And there might come a time when, if no indication was given, the balance sheet would no longer be a true and correct account

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of the company's affairs?—A. If you carry anything to its extreme, you may get a wrong position, I agree. Q. I only used your own phrase. There might come a time?—A. Yes."

Then he was asked: "Q. Supposing that time comes, a time has come when an indication is necessary, the indication must be sufficient, must it not, to turn something which admittedly without it would be untrue and inaccurate into something which is true and accurate?—A. I feel that that is a question that a chartered accountant could answer better than myself." With great respect, it seems to me a question which the chairman of the company ought to answer. Then: "Q. You have already told me, and we both agree, that a time might come—I am not discussing at the moment whether it had come in this case or not—but a time might come when an indication ought to be given to the shareholders of the utilisation of secret reserves?—A. It might come, I agree." Then he is asked to assume that such a time in a given case has come, and the question is put: "On that assumption do you agree that the indication which must be given to the shareholders must be a sufficient declaration to turn something which would otherwise be untrue and inaccurate into something which is true and accurate?—A. It is always a question of assumption. I feel that that is a distinct question." Then Lord Kysant says when he is dealing with the law he consults lawyers and gets the best opinion he can. There are a great many questions and answers which I do not think it is necessary to read. He was asked this: "Q. Never mind whether perhaps we arrive at our conclusions by different reasoning so long as we both agree in the conclusion that the accounts in respect of that year"—that is to say 1926—"had to give an indication to the shareholders?—A. I agree. Q. Do you agree that in the absence of an indication to the shareholders those accounts would have been false and misleading?—A. They would have been false and misleading if one had not drawn £150,000 from the reserves." Of course, the drawing from the reserves was a drawing from the open reserves, and the question which was being asked was with reference to the utilisation of secret reserves. Then Lord Kysant was asked: "Q. Do you see the words 'Adjustment of taxation reserves'?—A. Yes. Q. Do you attach any, and if so what, importance to those words?—A. Those words were suggested to me and I saw no objection. I did not go further than that. Frankly, I am not an accountant, and the big item was, in my view, absolutely one of the earnings of the company in that year. Q. Let me put my question again. I do not think you quite followed it. I am asking you as a very experienced man?—A. Not an accountant. Q. Not an accountant; you have said that already?—A. Yes, you repeated the other thing. Q. I am asking you whether you attached any importance, and if so what, to these words, 'Adjustment of taxation reserves'?—A. No, I did not go so far as that." Then a little lower down he says he thinks the ordinary investor would attach some importance to them. "Q. What importance do you think he would attach to them?—A. I am not qualified to answer that. Q. Would you

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yourself, with your financial knowledge and experience, have attached any importance to them?—A. I have already told you the moment they were suggested to me I agreed. Q. That, Lord Kysant, is not an answer to my question. Would you have attached any importance to them?—A. I should have attached some importance to them. Q. What importance would you have attached to them?—A. You are asking me questions that would be much more suitable to be dealt with by accountants of some description." Then a little further on he says "A. If you put it that way, I should say that I certainly attach some significance; I think that is the word you used. Q. Yes?—A. Some significance to them, but the extent to which anybody might attach importance to them I really am not in a position to answer." Then there is other evidence to the same effect.

SIR JOHN SIMON—The next answer is: "I would simply attach to them what it states, that there was an adjustment of taxation reserves."

MR. JUSTICE WRIGHT—Yes, thank you. That being, as it were, the starting point of the inquiry, what are the facts which you have to consider? The facts have taken a great deal of time to elicit, but I am not sure, now that we have got to the end of this inquiry, that there is very much mystery or very much complication. The broad outline is quite clear, and there does not seem, so far as I have followed the evidence, to be much difficulty. Of course, you are the judges of the evidence; you have heard it all. So far as I have been able to follow, there is no doubt at all that during those years, 1921 to 1927, the company was not earning any profits. It was both a ship-owning company and a holding company, and therefore profits might come to it in two ways; they might come to it in the form of a balance of earnings over expenses in running its own ships, or it might earn profits from the fact that dividends came to it from various concerns in which it held shares. In the case of six companies it held all the shares. I do not remember their names, but I shall say a word about them in a moment. In a number of cases, as a matter of fact in 30 subsidiary companies, it held in some cases a controlling interest, and in other cases shares, and in those cases, in so far as they paid a dividend, it derived a certain income; but after bringing these into account, and bringing in the general result of the ship-owning business, there was generally a deficit—not always. Then you have this position: that the company, although it paid its debentures, and although it paid its preference shareholders and ordinary shareholders, and did so without a murmur of complaint, except a general reflection on the hardness of the times, was all the time drawing sums which in the end, in the aggregate over seven years, amounted to £5,000,000, and it was disbursed in that way. As you remember, the preference shareholders and the ordinary shareholders had 5 per cent., which amounted to, very roughly, £700,000 a year gross. It has to be borne in mind that these dividends and interest were paid after deduction of income tax, and the more dividend the company paid the better off it was at once, because whereas it paid

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its shareholders without deduction of income tax it was able to keep the income tax itself, and, therefore, during all these years in which these dividends, so called, were being paid, you had a regular yearly credit which was put in the books to what is called income tax reserve, which was simply the amount of the income tax on the dividends and interest paid, and, as you know, it kept that because it was not bound to pay it to the shareholders, nor was it bound to account for it to the Government. That, as I follow it, was in the main the constitution of one of these accounts we have heard a great deal about, which was called in the books the income tax reserve. That account contained some minor credits, or some credits of this nature, credits for refund of income tax which had been paid in earlier years and paid in excess of assessment on profits, and when the actual profits were ascertained it was found that the assessment was excessive, and, therefore, sums were repaid back. That was under section 34 of one of the Income Tax Acts. Then out of that fund, the income tax reserve, there were some other payments in the nature of repayments in connection with excess profits duty. That was one main line of credit in the books of the company, and that was a credit in the main which was a form of credit which was abnormal in this sense, that it only applied if and to the extent that the company was not liable to pay income tax to the authorities because it was making no profits; but meanwhile it was paying these sums either to debenture-holders or to the shareholders. There were, however, other sources from which these heavy payments were made—I mean other than actual earnings or profits of the company—and the main of these is what is called excess profits duty reserve. I made a short statement about that, and I think you have yourselves Exhibit No. 117, which sets out very conveniently the whole of this history, and, so far as I know, sets out accurately the whole of the history of these excess profits duties. It was put in by Mr Manning, and he summarises it in this way. You will remember what the excess profits duty was. I say you will remember it, but, anyhow, it has been explained so often that I need not explain it again. When the war came to an end and the period of excess profits duty came to an end, the position had to be considered, because there were very many questions of great difficulty which had to be determined. The course which this company had adopted during the war years was to lay by year by year a sum of money in anticipation of what they had to pay, and, finally, I think the main reservation of these funds took place, but the actual process does not matter, because, finally, in 1921 in the books of the company they had put down as provision for excess profits duty during the whole period in which it was payable, ending in 1921, a sum of £2,260,600, and in fact there was paid over to the Revenue for the period with which we are concerned—I think the last payment was in 1921—a sum of £1,148,155, and, therefore, they kept in hand a difference of something like £1,100,000.

Now, there were considerable difficulties, as I have said, in ascer-

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taining the precise amount, and there were considerable difficulties in appropriating to each year the proper amount even if it was otherwise ascertained, because the duties differed in different years. But by 1923, as I follow Mr Manning's evidence, it was pretty well known what the ultimate liabilities would be, although in fact the ultimate liability was never definitely ascertained until May of 1927; but as it was fairly well realised, and, indeed, as it turned out, in that respect correctly so, the company it was said was justified in drawing from time to time or transferring to profit and loss from time to time the sums which in that way had been put aside, and these sums fell into two categories, a category of moneys actually paid, and a category of moneys kept in hand. There was a further complication which was not disposed of until 1926, and it was that the Government allowed in respect of the war period large sums to shipping companies, such as the Royal Mail Steam Packet Company under two heads, one called obsolescence, and the other called deferred repairs. You know what was meant by that, and I will not repeat it; and when they were settled in 1926 they were settled at a total of £1,428,705. Then when the excess profits duty was settled, it was settled at £1,769,122, and, therefore, when these two sums were set off one against the other, the final liability against the allowances for obsolescence and deferred repairs, the balance remaining was £340,000 odd. Now, that being the general position, I will ignore the constructive settlement in 1926 when no cash passed. That was ignored by Mr. Matthews when he made up his accounts, and, therefore, what you have to deal with for this purpose is first of all the balance of the money which the company never paid over to the Government at all, and of that they felt entitled to use, and did use, the sum of £400,000 in 1922. In 1921 they transferred £300,000 by writing it off investments, and in 1922 they transferred £100,000 to profit and loss. In addition to that, they did receive from time to time from the Government various payments until the Government had repaid them, as they did in 1927, the total amount that the Government had received in excess of £340,000. These matters are set out very clearly in the table. In 1923 they received from the Government £250,000 and transferred to profit and loss the amount of £100,000. In 1924 they received a further £390,000 and transferred to profit and loss £330,000. That left, as you see, a substantial balance, which appears in the accounts to the credit of the fund. Then in 1925 they received nothing, but they paid over £300,000 because certain claims were either actually settled or in process of being settled. In 1926 they received £270,000 from the Government, that is to say, on account of this fund, and then the account being considerably in credit they transferred to the profit and loss £550,000. In 1927 the fund was finally closed up, and at the final closing up there stood to the credit of the fund £232,788. So that in all these years there was available on this account £1,912,788, and no part of that money was money earned during the period in question. It represented in one sense, though perhaps not technically, moneys which had been appropriated during the war

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period. It may be I am a little in error as regards 1921—I will refer to that in a moment—because there was paid over in 1921 to the Treasury in respect of excess profits duty £125,000. That is part of the first item paid to the Revenue. That was not earned in 1921, but the payment was made then. There has been a great debate as to whether it is to be regarded as reserves or not, and that is a matter on which Sir William M'Lintock was severely taken to account; but everybody always called it reserves, and for the purposes of this case—I do not know what you think—it does not seem to me to matter what you call them; they were in fact not current earnings; and as Sir William said: “All I was looking after was what were the current earnings, and these were not current earnings; I noticed the amounts because I had noticed that they appeared in the profit and loss account, but they were not moneys which were earned in the period before 1921.” It may be, of course, that they were not available for use except at the time when they were actually used. Mr Matthews says he kept it because he kept this fund, and he had an idea from time to time how much he was to release to profit and loss account, and he indicated that to Mr. Cason, and Mr. Cason, as we shall see later, apparently conveyed that to Lord Kylsant. But they were, as you see, certainly not current earnings, and they were no criterion of the earning capacity of the company at all in the period in question; and it is a fact that, whether they are called reserves or not, you will have to consider whether these sums of money are not, for the purpose of the question you are considering, just as if they had been reserves, although they were, as you see from this account, from time to time becoming available for use. Then you will consider this question, whether the essence of the matter is simply this, that the shareholders ought to have been told that the company was being kept going by means other than current earnings.

You have been referred over and over again to this Exhibit 21, and I think you know all the figures in it probably very much better than I do, and I am not going through them again. I will just say a very few words about it. I have referred, as I thought I ought to refer, to these two big items which come in time after time, the income tax reserves and the excess profits duty reserves, and I think, as you have heard the evidence, you can quite appreciate all that was to be known about these. In addition to that, you find in 1921 a very large sum of money, £1,120,452, brought into account from three of the subsidiary companies. The three companies in question are not what are called the 100 per cent. subsidiaries, but they had accumulated, presumably as the result of the war, that sum, and that bonus was brought into the profit and loss account as a profit for the year. It may be said that in one sense it was a profit of the year, although it represented earnings on the part of the subsidiary companies for some abnormal years preceding. It was brought in, however, and there was a payment out to the Revenue of £125,000, which is put as a special debit. Then you have a balance on the voyages account. Before you deduct the general expenses, which are set out here, after deducting the running



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expenses you have a balance on the voyages account of £825,890, but as against that you have to set off the general administration, general repairs and maintenance, the insurance fund, which of course is a reserve, and depreciation of the fleet, which is on quite a separate if not a different scale, and depreciation of premises, and the special debit of £125,000. It is said that that special debit ought to be set off against the special credits, and that the figure of deficit, which appears as £904,000, ought to be reduced proportionately. That may be so. It does not seem to make any difference in the final result. Then you bring in the interest on investments, and then you have the special credits which, as I understand the view put forward by the defence, ought simply to come in along with, and on the same footing as, the interest on investments. That is the year 1921.

In 1922, again, you have certain special debits which, it is said, ought not to come in where they do but come in lower down, and in that way reduce the deficit of £570,000, but again the result would be the same. The result would be that after bringing in the £809,871, and the interest on investments, and deducting the running expenses, including depreciation, you would have, as appears here, the total surplus obtained, by using £100,000 of excess profits duty, of £45,000.

Then 1923, 1924, and 1925 I need not trouble to refer to specially. In 1926 you get a position which, according to this table, shows a surplus on the whole of the position of £628,535. That surplus is only obtained by bringing in excess profits duty, £550,000; income tax reserves, £175,000; profit on the Nelson Line and the general reserve fund, £350,000. That is the first of the two years with which we are concerned; and in 1927 you have a very similar position, subject only to this, that the excess profits duty is finally exhausted in 1927, and the income tax reserves, profits on steamers and premises sold, corporation profits tax, and sundries, make a total of £540,386. Then in that year there was also brought into the account the bonuses of £300,000 obtained from the two Nelson Companies, under circumstances which I am sure you fully remember. The Nelson Companies had been prosperous; they had had this money available, and they paid it over in the form of bonuses which they declared in that year. Whether the company benefited by that payment of money except as a matter of book-keeping, by the fact that it received a cheque and then parted with the same amount by another cheque, I am not very clear. But, as you will remember, when the bonus was declared and the cheques for the £300,000 were paid over, there was a further concomitant transaction under which the Royal Mail Steam Packet Company sold to the Nelson Steam Navigation Company the shares which it held in the other Nelson Company, H. & W. Nelson, that is to say, all the shares, and purchased from the Nelson Steam Navigation Company 1,000,000 ordinary shares which were then created, and as to a half were dealt with as fully paid up. That part of the transaction you will remember fully. I do not think it concerns this case very much, except that, although it is clear the £300,000 was paid over by cheque, it does appear that very shortly afterwards, although it came into the 1927

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accounts as a credit, it was retransferred to the Nelson Company in completion of the transaction to which I have referred. Now, I think that is all I need say about this table which you have considered and pored over and deliberated over, and you have, I believe, had the satisfaction of taking it home with you from time to time; no doubt you know all about it; and all I want to do is to explain, as I think I am bound to explain, so far as I understand it, the general position.

Then as to the subsidiary companies, you will remember that the Nelson Companies seem to have been rather prosperous. The M'Andrews and M'Iver Companies were less prosperous, and, indeed, paid no dividend in 1926 and 1927. The two big companies, the Pacific Steam Navigation Company and the Royal Mail Meat Transport Company, are dealt with very shortly by Sir William M'Lintock, and I will just remind you quite shortly of what he said. Mr. Gill also gave evidence about the Pacific Steam Navigation Company. I think it is necessary to know something about the position of the subsidiary companies, so far as it is in evidence, because we have no evidence apart from these bonuses as to what the actual position of the other subsidiary companies was—for instance, Elder Dempster and the Union-Castle, we know nothing about—but as regards the Pacific Steam Navigation Company what Sir William M'Lintock says is this. He produces the copy of the report which I think you have seen. This is what he said when he was examined by Mr. Pritt. "Q. Coming back to the figures in 1926, the company's accounts, as now, indeed, we can see from that report, showed a profit after charging depreciation of £60,532?—A. Yes. Q. That is arrived at by taking the balance available, as it is called, £80,858 3s. 8d., that is balance available on the right-hand side of the profit and loss account. If you deduct from that £20,327 4s. 7d., which is the balance brought forward from 1925, you get £60,532 as the profit for the year. Is that the right way to deal with that?—A. Yes. Q. So the actual trading loss for the year"—and then I do not think I understand this. He says here that the actual trading loss, I think after charging depreciation, was £83,755; but I will go on, because I may have to refer to that again. Then he was asked: "Q. The difference between plus £60,000 odd and minus £183,000 odd is £244,287?—A. Yes. Q. How was that figure made up?—A. Profit on the sale of vessels, £11,241; transferred from obsolescence account, £148,000, and a transfer of what we described as 'sundry credit balance not required'; these three items together make a total of £244,287. Q. Do any of those items fall within the classification of reserves?—A. I suppose the obsolescence account might be considered a reserve and the £85,000 is probably a credit balance on which there is no liability, and it becomes a reserve. Q. I think in that year a dividend was actually declared and paid to the Royal Mail Steam Packet Company which absorbed £60,000?—A. Yes." And then he says that 1927 was much the same; it showed a profit of about the same figure, and then in fact there was a loss on the year's trading. The profit which is shown is, according to his evidence, constituted by various credits from various exceptional accounts not dissimilar from the accounts which you have

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been considering in Exhibit No. 21. You have had, I think, copies of those accounts, and I do not want to go into it in any greater detail. What is said, and it is rather a point which may not be very material for your consideration in this case, is that, anyhow, the Pacific Steam Navigation Company was paying its dividend and paying its interest, and so forth, not on its earnings, but on those special credits, whether they are called reserves or not, which arose from and appertain to the war period. I do not think I need discuss that in detail, because you will remember, no doubt, the evidence. It is really a subsidiary matter in this connection.

Now, as I say, you are concerned with those two years, 1926 and 1927, specifically, and you will remember that the balance sheet was duly signed year by year by Lord Kysant as chairman, and there is some evidence illustrating the manner in which the policy of paying dividends and dealing with the funds of the company was considered between himself and Mr. Cason. You will remember there was a document produced which you had in the exhibits—Exhibit No. 6—called “Estimate for 1926.” It is a document which was produced by Mr. Cason, and, as I mention Mr. Cason, I may say, in passing, that he seems to have been an extraordinarily careful and conscientious official—one of those officials on whom the success or even the existence of these big concerns depends, with a very long-established service in the company, where he was the chief accountant for a good many years, and he produced these documents which he said he made for Lord Kysant. As I understand it, the question was, what funds could be provided to pay a dividend on the ordinary shares of 4 per cent. in view of the actual financial position of the company? And this account was prepared and discussed. It shows the debenture interest, the preference dividends, the insurance account of 3 per cent., which, so far as one can judge from Exhibit No. 21, was somewhat excessive, depreciation of fleet, interest and discount, and it shows a total amount wanted of £1,476,500. It shows voyage accounts, receipts, less expenses, £265,000; that is budgeting for a profit, not after depreciation, because depreciation, as you see, appears on the other side of the account, but apparently after not only the various running expenses, which would figure in a voyage account, but all those general administration expenses which ought to come off the earnings. Then it says: “Sundry receipts, including interest on investments,” and that appears to be rather excessive. And it shows on that basis a deficit before any provision for ordinary dividend at all of £1,100,000. The problem which was being discussed was where to get the money from, or the credits from, for that purpose. It was suggested, as appears here, that the unpublished reserves—these are items which we have been discussing and which appear in Exhibit No. 21—were £600,000; they were to be drawn on to that extent. Insurance premiums were to be £100,000 carried forward, and then there was investment depreciation reserve £300,000. To make up the £1,300,000, it was proposed that the bonus shares from Nelsons, which were afterwards dealt with in the following year, should be brought into the account. The £600,000 was to be made

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from the unpublished reserves in this way: Income tax reserves were to contribute £160,000, eventually they contributed £175,000; excess profits duty was to contribute £350,000—and that, as you know, was altered to £550,000—and it was decided not to take the bonus shares in that year. Then there were various other minor matters which do not appear to have been actually availed of when the accounts were finally made up. In that way, with the £600,000 and the other items, and the £200,000 bonus shares of Nelsons, it was intended to find sufficient credits or funds to pay the outgoings after depreciation.

That is the discussion which was relied on by the Crown as showing that Lord Kylsant was completely familiar with what was happening, and that he was seeing how he could provide the necessary funds in order to pay the various expenses and pay the ordinary dividends. The balance sheet for that, as you remember, was eventually published; it is part of Exhibit No. 1. You will remember I said you will not for a long time forget the appearance of these balance sheets. It shows in the balance sheet. Sundry balances, accounts not closed, and debts owing by the company, including loan from company, £2,842,440. Now, the make-up of that sum, though no doubt perfectly understandable by an accountant, is a little puzzling to the ordinary person, because there you have put together not only debts owing by the company but you have those credits which are constantly being called reserves and the exact nature of which you know, so that you have lumped together in one sum moneys held by the company and debts owing by the company, and, to make an observation which is true, so far as I understand, of every one of these accounts, no one reading these accounts, even if he could understand "Accounts not closed," as meaning reserves, could tell how much was reserves and how much consisted of debts. However, that is true of all these various balance sheets, and it is not a point which is specifically complained of, although it has to be taken into consideration when you are determining, as you must determine, whether this balance sheet and profit and loss account is on the whole misleading and false or not.

Now, when you look at the balance sheet, bearing in mind exactly the position of the company, you find a balance for 1925, dividends paid in June, balance for the year, including dividend on shares in allied and other companies, adjustment of taxation reserves, less depreciation of fleet, £439,212, and there are various small items. You then find transferred from reserve fund £150,000, and you get the total £773,492, and that is expended in paying interest on debenture stock, interest and discount, dividends on the preference stock, surplus in favour of the company, proposed to be paid 4 per cent. on the ordinary stock, £200,000, and to be carried forward £66,000. That leaves a balance, and the account squares in that way. There you have the balance sheet which requires your consideration. You will remember that up to 1923 this balance sheet contained the words, "Profits for the year," and then it was considered better to change it to "Balance for the year," because, apparently, it was realised that truly there was no

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profit, if you merely look at the ordinary outgoings and incomings. It says: "Balance for the year, including dividend on shares in allied and other companies, adjustment of taxation reserves, less depreciation of fleet, &c." Whether the "&c." refers to the "less," or whether it refers to the positive items and not the negative items, is not worth considering, because I should think it clearly would read. "Dividends, adjustment of taxation reserves, &c.," and the "less depreciation of fleet" is a parenthesis. Looking at this document, in view of all those circumstances, you have to decide whether or not in your opinion it is a false document.

I am not going to repeat what I have already reminded you of, namely, that the time had come in 1926 when the state of the company was such that the company ought to have been informed either by the auditor or by the chairman that the concern was not paying its way apart from these special credits. For instance, as you see, £550,000 was taken from excess profits duty, and that was necessary in order to pay interest on the debentures, interest and discount, a total of £273,000, a further amount of dividend on preference stock of £233,000, and then dividend, interim and final, amounting to £350,000. It is perfectly true that it shows a transfer from the reserve fund, which would seem to indicate perhaps that it was the only substantial use that was being made of the reserve, as, indeed, it was the only use that was being made of the published reserves, and it is perfectly true that you have these words "adjustment of taxation reserves." That is to say, the word "reserves" occurs twice on this page, and that may be some sort of indication to any one who understands the use of this language that to some extent other reserves than the published reserves were being drawn upon. On the other hand, it is pointed out that the amount drawn from taxation reserves which figures under the word "Adjustment" is a very heavy amount indeed—£550,000—and it is said, in view of all the circumstances, to make that anything but a misleading document, in view of the large amount drawn from reserves in proportion to all these other figures, that ought to have been clearly and specifically indicated, so that the true position of the company could have been disclosed to the shareholders; and that in view of the fact that it ought to have been disclosed, and that the accountant signed his certificate, which may be is only limited to the balance sheet, but which is generally understood to refer to the profit and loss account, which would be incorporated in the balance sheet—in view of the fact that he signed the certificate, it is said, and it is for you to consider, that that is not anything other than a written statement, false in a material respect, because it conceals the true position of the company in that year from the shareholders, who are entitled to be told, and to whom this report is addressed.

This seems to be the material on this aspect of the case relevant to 1926. In 1927 there is a similar exhibit—Exhibit No 14. I do not think I have got the precise date for the moment on which that was discussed. It appears in Mr. Cason's evidence. I do not know that he gave the date. Anyhow, it was discussed at some time with reference

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to the 1927 figures, and that shows in a very similar way the arrangements that were being made, the provision which was being made to provide enough money to pay the debenture interest, the preference dividend, and to pay a dividend of 5 per cent. Of course, in a sense the debenture interest had to be paid, it was a first charge on the assets, but there were other questions, the question of paying a 5 per cent. dividend, and, in a less degree, the question of paying the preference dividend, in view of the circumstance that dividends are generally paid out of profits and ought to be paid out of profits. They may to some extent be paid out of a past profit stored by, but, in the main, dividends, it is anticipated, are being paid out of the profits, and in some degree it may appear that when you have a balance sheet showing, as you do, a 5 per cent dividend, not for one year, but after a long sequence of years, and, indeed, rising to 5 per cent. after payment of 4 per cent. in a previous year—when you have those circumstances, and you have such a balance sheet and such a profit and loss account as you had, which is in terms just the same as for 1926—when you have those circumstances, again, it is said, that this is a false and misleading document. Of course, you have to consider that. I do not know that there is any other material on this first point of the case that I can usefully refer to.

The next thing, of course, and the most vital and serious and important issue in this case, is the question whether, if you find that this was a false and misleading document, it was published knowingly and with intent to deceive. That is a question of fact for you to infer from all the circumstances. It is a question of fact which requires the most careful consideration, and it is a question of fact as to which I need not remind you again the maxim peculiarly applies that a defendant is entitled to the benefit of the doubt. You have to consider all the facts.

I may remind you that there was, as we see from the balance sheet of 1911, a rather stereotyped or traditional form of balance sheet which was published by the Royal Mail, and when you get to these later years the same compendious form of balance was continued, with some variations. Well, that is a matter to be borne in mind. It is also to be borne in mind that in the years 1926 and 1927 circumstances were changed.

There is another matter to which you may give some attention, and that is that though the chairman took obviously an active part, not perhaps in the actual preparation of the balance sheet, but in the determination of the manner in which the accounts of the company should be handled, and actually signed the balance sheet, and, therefore, made himself responsible for it, he had associated with him as colleagues a board of directors. As to the position of the directors, it may well be that if they were honourable men, and were cognisant of all the circumstances, that is a matter to be taken into account in considering the position of Lord Kylsant. But, so far as the directors are concerned, they are not before the Court in any sense, either as parties or as witnesses, and it is an elementary principle of justice that no

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opinion, certainly no adverse opinion, should be formed against any person who is not actually before the Court and in a position to state his case. What their position is you may or may not have an opinion about, but it is not an opinion which can be based on evidence, whatever it is. The only evidence about the position of the directors and their actual cognisance of these matters relevant to the balance sheet, so far as I remember—and, of course, the whole evidence is present to your minds—is the evidence, on the one hand, of Mr. Cason that he never heard it discussed while he was present—of course, he cannot speak as to what happened when he was absent, and apparently he was present when the accounts were brought before the board—and, on the other hand, there is the evidence of Lord Kylsant that the matters were discussed with the other directors. You have heard exactly what he said, and I will not repeat it.

In these proceedings the sole question is as to Lord Kylsant himself, and apart from the question which I have just mentioned as to the character, as vouched by Lord Kylsant, and the names of the directors, whom some of you may know, you have to consider the position of Lord Kylsant as having signed the balance sheet quite apart from what any one else may or may not have done. He is the only person before the Court, and he must be responsible for his acts; whether for good or evil, they are his acts. That is all I want to say about the directors.

As for the balance sheet itself, of course it is obvious to all of us that if it becomes known to the world that balance sheets of companies are not things which can be relied on, that is a very serious matter for the national affairs and commercial affairs of this country. But as I have already pointed out, these general considerations are not of value to you in determining the specific question, namely, whether there was a misleading balance sheet, and, if misleading, was it misleading to the knowledge and realisation of Lord Kylsant; and if that knowledge and understanding was present to his mind did he then publish it with the fraudulent, wicked, and criminal intent which the law requires to constitute the offence? Matters of intent are matters which juries have to determine in every action of this character. The charge is a charge of fraud, fraudulent intent, and in a sense it can only be decided by a jury as a matter of inference from a consideration of all the relevant circumstances. So far as the other evidence is concerned, those are the relevant facts which have occurred to me, others may occur to you, for consideration. I do not know how far it is in any way definite or tangible at all in this connection, but you have the fact that if the dividend was 5 per cent. certain remuneration became due to Lord Kylsant under his agreement, and was in fact collected by him in 1927. It was not collected in 1926, because it was not due, because the dividend was only 4 per cent., and in 1928 he did not collect it, though it was passed by the accountants. There is that circumstance, which is quite within your knowledge, and it is for you to determine what, if any, weight you should give to this matter.

In considering intent, it is always a question which juries consider in connection with possible motives. Without entering into any

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fine analysis, it is quite obvious that motive and intent are two different things. A man may have an intent for which no assignable motive can be given. On the other hand, a man may have assignable motives and yet he may not have the intent. One knows in these days of large commercial combinations the leaders of commerce who are in positions of importance may sometimes think of the affairs of the company rather in terms of the group, as it is called, than of the company itself. That, *prima facie*, is an evil, because after all, however many companies may be associated in a group, and however much they may be under the control of one man or a body of men, still the primary duty in law is as between the board or the directors and the shareholders of that particular concern, the people who have invested money in that concern. So that if you are looking at motives the motives may be of a somewhat complex character. It may be the motive that the chairman of a concern may feel that he ought to keep the flag of his company flying until a certain stage is arrived at, when the flag must be lowered, or to change the metaphor, in the old sailing ship days the captain of a ship may carry on full sail because he is anxious to reach his destination, and may overstep the mark and lose either his sails or his masts, or both. The question of motive, therefore, in a case of this sort may be of a very complicated character, and you must, as well as you can, weigh all these considerations, because, as I say, intent is a matter of inference from all the facts and circumstances of the case.

You, of course, have heard the evidence which Lord Kylsant gave, which I am not going to repeat in detail, because you heard it both in chief and in cross-examination; his evidence is in your recollection, and, as I understand, it may be summarised perhaps imperfectly, in this way. His view, as I understand it, as stated by him in his evidence, was that there were a series of trade cycles, and that when you came to these critical years, 1926 and 1927, the cycle had been on the down grade, had changed in direction, and was tending towards the up grade. 1926, he says, started in the trough of a wave. 1927 he said was better than 1926, and, therefore, even then, and under all the facts of the case, he felt he was justified in carrying on. He does not, as I follow it, deny that the time may have come—I am not sure that he is very explicit—for giving information to the shareholders beyond the mere fact of the dividend, but, as I gather, he says he left the exact form of that information to the accountants, and was satisfied with what they did. These and other circumstances, which will be present to your minds, because you have heard the evidence, may be very material. No doubt, it was important to keep the status of the company and its reputation unimpaired so far as he could, because of this guarantee which we have heard about, which had to be extended in 1929, and which he hoped would be extended in 1929. I might, of course, read the whole of his evidence, but unless I read it all I do not think I could give a complete account, and you must rely for the details of that evidence, and any explanation, upon your recollection of what you heard him say. You have seen him in the witness-box; you have heard all his explanations; and you have had an opportunity of forming



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an opinion as to his personal attitude, as a matter of human understanding and human knowledge.

I do not really think on this matter, which is so essentially a matter for you, I can really help you any further. You will bear in mind that there are the two questions. If you think this balance sheet was published in such a form as to be misleading, then you have to ask yourselves, did Lord Kysant know and realise that it was misleading? The fact that he ought to have realised it, of course, is only one element, if you think he ought to have realised it; and, secondly, if he realised that it was calculated to mislead, did he deliberately, wickedly, publish this with the intention of misleading and deceiving the shareholders in the concern in terms which cannot be disposed of by saying it is no use being wise after the event? Because, of course, if you have an experienced and very able business man with knowledge and realisation of facts, he is assumed to know, and he must know, all those circumstances which are only elicited in the course of this long and laborious and trying inquiry which has been necessary in this Court. Of course, you will remember this now that things have happened. It may be that, however experienced and able a business man he was, he may not have appreciated exactly all that was involved or might be involved in what he was doing.

I am going to leave this issue to you without further words, because I do not think I can help you any further. It is not a matter for my decision one way or the other; it is a matter for your decision. You must apply your minds to this question, as to the other serious questions in the case, without fear or favour or affection; you must apply your minds to the question truly and indifferently, if I may use the old phrase, which it is sought to change, in the old Prayer Book—it is still a phrase used in these Courts—truly and indifferently, that is to say, making no difference on the one side or the other in the sense of partiality or leaning, but simply acting according to the evidence and according to the best of your judgment and conviction, and as your conscience requires you to decide. That is all I want to say about the charges on the first two counts as affecting Lord Kysant. I am sure I need not remind you that in all criminal matters a charge must be established beyond any reasonable doubt. That does not mean, of course, that certainty is possible in human affairs; it merely means that if the matter is left in a reasonable doubt, if the balance of your mind is left without being certain one way or the other, then the benefit of that must go to the accused man.

Now I pass to the prospectus. You have, of course, copies of the prospectus, and I have no doubt you have the relevant facts fixed in your memory. There are certain matters which, perhaps, I ought to refer you to, though I am not going to read the prospectus as a whole, but I must again draw your attention to certain passages, which I have no doubt you have duly underlined and, as I say, have fixed in your recollection. Here is the prospectus. So far as I am going to read it, it begins by setting out the constitution and objects of the company. I am not going to read the first page; it refers to the combined fleet. Then

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these are the words to which your attention has been drawn, and to which your consideration must be carefully directed :

"Although this company, in common with other shipping companies, has suffered from the depression in the shipping industry, the audited accounts of the company"—that is, the series of balances—"show that during the past ten years the average annual balance available (including profits of the insurance fund) after providing for depreciation and interest on existing debenture stocks, has been sufficient to pay the interest on the present issue more than five times over. After providing for all taxation, depreciation of the fleet, &c., adding to the reserves, and payment of dividends on preference stocks, the dividends on the ordinary stock during the last seventeen years have been as follows,"

and then they are all set out, and they are set out accurately. As you see, the average annual balance available is stated to be that expressed in the audited accounts of the company for the ten years from 1918 to 1927.

Of course, it is perfectly true that these balance sheets do show these average annual balances, that is to say, if you put them down separately and make the necessary adjustments after providing for depreciation and interest on the debenture stocks, and then divide the total so arrived at by 10, you would arrive at the average annual balance as being more than £500,000, because, of course, the five times over is £500,000. That is absolutely correct. Then it goes on: "After providing for all taxation, depreciation of the fleet, &c., adding to the reserves, and payment of dividends on the preference stocks." Then it gives the dividends on the ordinary stock, which are correctly stated. It is perfectly true all taxation during those years had been provided for, including excess profits duty. Depreciation of the fleet had been written off year by year on a basis which we are told is liberal, 5 per cent. instead of 4 per cent., which was in some respects customary. "Adding to the reserves"—if that means reserves of capital, as presumably it does mean—if that means the published reserves, that again is perfectly true, because I gave you the figure of the reserves in 1911, when the company was a very much smaller company. It was a small figure—I have forgotten the amount—but in all, insurance and general, it was something like £420,000, whereas at this date the published figures, after taking off £180,000 in 1926, were still something like £2,760,000. You remember the precise figure, which of course can be found in a moment by looking at the balance sheet: reserve fund, £1,450,000; insurance fund, which is known as a true reserve, £1,311,000; so that all that is absolutely true.

Sir JOHN SIMON—It is shown in the prospectus, my lord.

Mr. JUSTICE WRIGHT—Yes, it quite correctly appears there, and it appears in the balance sheet for 1927, and there is no question that it is perfectly correct. Now, what is said is that though it is true, there is such an economy of truth as to deceive, and to deceive to his loss, and, therefore, to defraud, any intending investor, because it is said that though you have these annual balances shown on the profit and loss account, and though you have these dividends paid year by year, yet that gave no true account at all of the actual financial position of

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this company in the latter years of this period which is averaged. It is said that if instead of averages you had put year by year not the average annual balance available, as appearing in the balance sheet, but if you had put in your prospectus something entirely different, namely, a statement year by year of the profits as they accrued, you would have had a very different picture, because in the bumper years up to 1920 and part of 1921 you would have had very large earnings and profits, and in the following years you would have had that state of things which you know and which I am not going to repeat. Well, of course, it may well be that if a man of scrupulous honour were asking a friend to lend money to this concern he would not have been content with a statement; he would have told his friend what the position was so that his friend might, on those facts, rightly make up his mind as to the true position of the company. The friend might have thought to himself, having that before him: "Well, here is a company which has certainly done very badly for some years, but the tide may turn at any moment. I am willing to risk it. I know what the assets of the company are; I know that there are these reserve funds, I know that there is a fleet, and investments worth, we will say, £8,000,000 out of £13,500,000, but probably as a going concern it is worth substantially more." If with all that in his mind he had said: "Well, I will take the risk," he could not have complained even taking that basis. It may be that you may feel that in a prospectus there ought to be a disclosure as complete and as fair and as candid as that. There are—and it is not in question here—certain things which a prospectus which asks for subscriptions to debentures must contain, but they are quite irrelevant here. That is a view as to what is fair, and I might also say as to what is honourable; but you are here dealing not with those things, but with the strict words of a criminal Act, and therefore you must examine the matter with different spectacles, I was going to say. Anyhow, you must bear in mind what is the question you are really considering in this case.

It may be true that this form of prospectus was approved by the directors at a board meeting or a meeting of the court, and although you may bear that in mind, you will also bear in mind that you are dealing with the actual responsibility of Lord Kylsant, and Lord Kylsant alone. Lord Kylsant has told you that he consulted a solicitor and counsel as to whether the prospectus was sufficient and correct. I suppose he was thinking of the prospect of civil proceedings; I do not know. It may be that this advice was taken because he was anxious not to deceive or defraud anybody. Lord Kylsant stated in his evidence, and no doubt it is the fact, that he himself on his own personal account subscribed—we are not told to what extent—to this issue and was allotted some debentures. There is no doubt that he subscribed, and that is put forward as showing that whatever he did was done in good faith. The issue, as we know, was over-subscribed. In addition to that, I should like to read a short passage in his evidence in which he was cross-examined about this prospectus and in which he states his view of the

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position. The Attorney-General, cross-examining Lord Kysant, asked the question :

"Now let me ask you, from the point of view of the prospectus, a few questions. As I said in the other matter, I am not going to ask you technical legal questions or technical accountancy questions"—the "other matter" is the account—"it would not be fair ?—A. Thank you Q. On the other hand, I am going to avail myself of your business knowledge and experience. I would like to ask you this question. Do you think that the duty of a person who puts forward a prospectus is to put forward all relevant facts fairly and squarely so as to enable an investor to form his own judgment?—A. Yes. Q. And you would agree, would you not, that it would be deplorable if that standard is ever departed from?—A. I agree. Q. And it would be deplorable if that standard is departed from by a man in a high and eminent position in the City of London?—A. I agree. Q. Did you put forward all the relevant facts in your possession to enable an investor to form his own judgment?—A. I put forward absolutely a true and correct statement. Q. That is not quite an answer?—A. And I took this step, that not only was it first passed by one of the leading solicitor firms in the City of London, but then at my request they submitted it to a leading counsel, and I said : 'Who is the best counsel to consult on this particular class of work,' and they mentioned the name of a distinguished member of the Bar and we got his opinion. Before that or after that it was twice before my colleagues and was very fully discussed, and in my view it was an absolutely straight, true, and fair description of the company."

Then the Attorney-General said :

"Counsel advises on facts before him. It is not very much good saying what Counsel advises unless you know what facts are put before him ; and the same applies to solicitors. For the moment all I asked you was this. Do you state to the jury that you put before the investor all the relevant facts so that the investor might have the material on which to make up his own mind? Did you?—A. I say Yes. Q. In fact the issue was very largely over-subscribed, was it not?—A. Yes. Q. And, of course, the issue is not in the nature of a gambling thing. Debenture stock in the Royal Mail would have been regarded as almost in the nature of a gilt-edged security?—A. At that time the security over and above the amount of debentures issued was over 14 millions, and even to-day—we are not discussing that to-day—it is many millions. Q. Then am I right in saying that it would have been regarded not as a gamble, but it would appeal to a steady investing public?—A. Yes Q. Amongst whom there would have been many persons in quite humble circumstances, in all probability?—A. There are always some."

That is all I think I need read at the moment, and, as I have reminded you, you have heard the evidence given by Lord Kysant, and, of course, it would be futile for me to read again the whole of that evidence. Undoubtedly you have listened very carefully, and you remember what impression it made upon you, taken as a whole. I read that passage as showing, I think fairly, so far as I can judge, the attitude of Lord Kysant on this issue. We have, of course, certain material as to what were the circumstances at the moment which may have had some influence in determining the issue of the prospectus at that time. You will remember the letters about the overdraft which the company had with Barclays and with Coutts, and, in addition, Lord Kysant says, as appears on the prospectus, that it was desirable to provide additional capital for the new freehold building which was being erected, and the general purposes of the company. Anyhow, there was that, and then you have heard in some detail the history of how the prospectus developed. It was Mr. Lewis who was in charge of the accountancy department, as I follow, at that time. You will remember

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that an overdraft was either granted or, perhaps more truly, was continued or increased, in 1926 and 1927, on the anticipation of a public issue. For instance, in December, 1926 (Exhibit No. 26) there is a letter initialed by Lord Kylsant as having been received on the 3rd December, 1926:

"With reference to your recent interview with the chairman and your letter of the 30th ultimo, we have pleasure in informing you that it has been agreed to grant the Royal Mail Steam Packet Company an additional £200,000 overdraft, making £500,000 in all, and we gather it is your intention to repay this additional advance within the next three months from the proceeds of a public issue."

That is renewed in March, 1927, on the same terms, and then there is a note in September, 1927, of an interview with the bank manager. This, I think, was spoken of by Mr. Cason. The second paragraph says:

"He called to remembrance that it had been agreed for a new issue to be made to clear off the overdraft and could only at the moment agree to extend the overdraft for a further three months when the question can again be gone into. I imagine that the bank may be disappointed because two White Star Line issues have been made in which their services were not required, as was the case in the last issue of our preference stock."

Then there is a further extension in December to June, 1928, and then there is a statement of the amount of the overdraft in Exhibit No. 31; Barclays was £466,000 on the 30th June, or would be, and Coutts was £471,000. That being the position, Mr. Lewis, in the absence of Mr. Cason, was called in, and the first form in which we have the prospectus is on Exhibit No. 32, and the original form was:

"The audited accounts of the company show that for the past ten years the average profits (including profits of the insurance fund), after providing for depreciation and interest on the existing debenture stocks, have been sufficient to pay the interest on the present issue more than . . . times over."

Then the figure is taken from the printed accounts. Of course, you know now how those figures were arrived at. Then an average is struck. Then, I do not know why, but there is some question with Mr. Morland's assistant about the arrangement of the annual figures. That is Exhibit No. 33:

"Mr. Morland's usual assistant reported here this afternoon later in order to go into the figures, and from what I gather he intends to carry the excess profits duty refund, the surplus income tax and other reserves, and surplus depreciation written off, from the years in which they appear in the printed accounts into the years in which they were earned. This means that Mr. Morland's figures will differ considerably from mine and will take him many hours to do."

Well, of course, if what was intended had been to publish their yearly profits year by year in the prospectus, it, of course, would have given the investor a degree of information which he would not have in the form in which the prospectus was published. Then, of course, all these inquiries which Mr. Morland's assistant was initiating would have been most relevant, and if that was the form in which the yearly profits were published the investor would have had a degree of information about

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which he could not, I imagine, have complained. But that was not the form which the prospectus took, and it appears that if Mr. Morland's figures, or his assistant's figures, had been adopted and elaborate adjustments had been made, putting into the earlier years all these matters which were afterwards brought into the later years, as you know, and brought in with the annual balances, still, the average would not have come out any different or at all substantially different. That, of course, is obvious. If you take an average, you may, within the period over which the average is taken, have very diverse figures, and I should imagine—I do not know, but one feels—that if ever I venture on a prospectus in future, I shall look very shyly, indeed, at any reference to averages. Indeed, I am not sure that under the new Act such a thing can be done. Anyhow, there is the fact, that the average is what was going to be published, and was published. Then there were various alterations and amendments which I need not, I think, trouble you with, because with one exception they are not really very material. Exhibit No. 43 is one of the intermediate proofs signed by Lord Kylsant on the 25th June, 1928: "Approved by the special court subject to slight amendments." Then later there was a further amendment. Exhibit No. 43 is later in date and represents a modified version as compared with Exhibit No. 44, because you see the alterations which appear to have been made altered in writing. In Exhibit No. 44 you get:

"The audited accounts of the company show that during the past ten years the average available balance"—this word "available" is supposed to have some significance; I do not know what—"the average available balance (including profits of the insurance fund), after providing for depreciation,"

and so forth. Then to that, again, a further addition is made which appears on Exhibit No. 45, because Exhibit No. 45 has an additional note—the insertion of a leaded type, or rather a change from the ordinary type to the leaded type—in these words "sufficient to pay the interest on the present issue five times over." That alteration is made from Exhibit No. 44 to Exhibit No. 45, as you see, and then there was also added this phrase to the last paragraph but one: "Although this company in common with other shipping companies has suffered from the depression in the shipping industry," and then it goes on "the audited accounts," and that is the form in which the matter was finally issued and issued with very considerable success.

Now, as I have already said, and I think it is obvious to anybody, as a statement of the real position of the company this prospectus does leave something very much to be desired if the investor was to make up his own mind on the actual facts. It does look as if it was carefully arranged and carefully prepared so as to put the best face on the position, and do so by stating a series of matters, each one of which was strictly accurate, but there are certain relevant matters which are crucial if the investor was to know the true position of the company; for instance, the circumstances under which dividends had been paid during all those years, the use of those credits or reserves which we

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have heard about, and, if it was realised by Lord Kysant, the possibility of the guarantee under the Trade Facilities Act not being renewed. These and other matters which are obvious were not stated. Here, again, you have got to consider very, very seriously this first and main question. Was the form which was adopted here, and which erred by reticence, deliberately adopted with an intention to deceive? Was it not merely a case of prudent and well advised reticence, but a case of malignant, deliberate, wicked, and treacherous deceit in order to defraud?

This is one of those difficult cases, but not impossible cases, which have occurred from time to time in the course of company transactions, where a document has been put forward in order to be acted upon (prospectuses and other things) and put forward in such a form, though it stated every fact correctly fact by fact, yet the true effect of what was said was completely false and completely misleading. That result might be achieved by a man acting with the best of intentions, and while his mind was fixed on attaining his object and floating an issue, and while he was in a sense thinking of what was the best way to achieve that object. He might, in fact, not be conscious to himself that he was going to mislead people, and that he was going to induce them to subscribe to the issue under a belief which was completely false and completely delusory. People sometimes say to themselves: "Well, this is all I need tell; I will only tell as little as it is necessary; but what I will tell I will tell quite accurately, and then I can quite fairly and honestly leave it to the person who reads this prospectus to make up his own mind." That is to say, he may have no dishonest intent, he may have perhaps no real consciousness that what he is doing is delusive and mischievous. He may, of course, be in some cases, if he is under a legal obligation to disclose all the relative facts, liable to a civil action. Here you are not concerned with the civil liability; you are concerned with the offence under this Act as stated in the indictment:

"Circulating a written statement, to wit, a prospectus inviting the public to subscribe to an issue of 5 per cent. debenture stock in the Royal Mail Steam Packet Company which he knew to be false in a material particular in that it concealed the true position of the said company with intent to induce persons to entrust or advance money to the said company."

Of course, that means that he fraudulently and with wicked intent deliberately published that with the wicked design of defrauding. That, again, is a question entirely for you. Do you think that this was a document which by accident or design, innocently or criminally, did mislead people? Do you think that people invested on the faith of this document, and in the belief that it contained all that it ought to contain, whereas, if they had been told the true facts they would not have put money into this concern at all, because they would have wanted some guarantee as to the earning capacity of the company? As we all know, though a debenture holder in fact is secured on the assets which, in certain events, he may realise—which he may enter into possession of in certain events—yet the ordinary man who takes debentures is not thinking of that.

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He wants to take a debenture which is secure as to the assets and which is also likely to be a useful debenture to him and yield him an income year by year, an income which will come in due course from the earnings of the company, and, therefore, it seems common sense that a man would not invest in a company at a time when it had a record of unfruitful working for some years past, however much it may have had of the special credits to keep it going and to provide dividends.

That may be perfectly true; but, as I say, you have to go on a step further; you have to consider anxiously, assuming that you are satisfied that it was in truth and in fact a misleading document, was it deliberately concocted, was it deliberately put together with the intention of stating certain things and not stating other things, so that any one reading what was said, not knowing what was not said, would be deluded and deceived as to the true nature of the company? It is said by Lord Kylsant that he knew what the position had been, he knew what the earning capacity had been, and he would say: "Well, there is a well-secured asset here," and then: "We are in the trough of the wave now, or we are just coming from the trough of the wave, and things will soon improve again, and then all will be well." That is a matter which you will have to take into account. You will bear in mind that it is always possible to be wise after the event; but, on the other hand, you will consider whether there was such necessity at this time for obtaining further money as to form a motive for deceit. Even that will not be enough. You must satisfy yourself, before you can find Lord Kylsant guilty, not only was there a motive, but was there an actual intention, a deliberate and criminal intention, to obtain from the investor money which he would not have parted with if he had known the true facts. It is not a question here whether what was done was done within strict business lines. It is not a question whether what was done was strictly honourable. It is a question whether an offence was committed under this penal section which carries with it in the event of conviction the consequences which inevitably follow from conviction under the criminal law. There, again, I do not think there are any parts of the evidence I can usefully remind you of: you have heard it all; it is a matter of judgment. You will bear in mind what I have said about having to be satisfied that the offence is made out beyond reasonable doubt. As to the actual words that were used, they have been criticised to some extent. It is said there is some positive misstatement here because any one who read about adding to the reserves might in his mind think there were no other reserves, and in a sense that is impliedly or by inference inconsistent with the actual facts as to the using of these moneys which we have heard about. Then it is said that the audited accounts were themselves misleading and known to be so, and the use of them in this prospectus would be some mark of evil intent. However, there it is. In the main it is quite obvious that this is, letter by letter, word by word, an accurate document, so far as it goes, and it can only form the basis of a charge of fraud if you are satisfied, as I have said more than once, that there was this deliberate



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and wicked and criminal intent to concoct a false and misleading document.

Now I pass away from that, and that only leaves me one thing more, that is the charge in the counts in which Mr. Morland is concerned, and which, as you remember, have to be dealt with quite separately on the evidence which has been given applicable to him. You must keep your minds, as I am sure you have done throughout in considering Mr. Morland's case, definitely clear of any matters of which you have heard which are peculiar to Lord Kysant, and which do not apply to Mr. Morland at all. The charge against Mr. Morland in the first and second counts is this: "The said Harold John Morland did aid, abet, counsel, and procure the said Owen Cosby Philipps, Baron Kysant, to commit the said offence." That is repeated in the second count. So the charge against Mr. Morland is that of aiding and abetting. It is different from a charge of conspiring with him to commit an offence, because on a charge of conspiring the prosecution have to establish an actual agreement, a concert between the two men who are accused. In this case aiding and abetting presupposes that the offence has been committed, and alleges that the accused man, with knowledge that the offence was being committed, aided and abetted, that is to say, knowingly and deliberately helped the execution of the design for the committing of the offence. In the old days a man could not be charged with aiding and abetting an offence until the principal offender had been convicted, because you cannot aid and abet another man to do something which the other man does not do. Therefore, if Lord Kysant did not commit the offences with which he is charged, the question of aiding and abetting cannot arise, because the question only arises when the jury are satisfied of the guilt of the man who is charged as the principal. Therefore, these matters, as far as Mr. Morland is concerned, only arise in that event; but, of course, if you are satisfied that Lord Kysant was guilty of these matters charged against him in the first and second counts, then you would go on and consider whether Mr. Morland, with the same guilty intent, knowing what Lord Kysant was doing, and knowing his guilt and wickedness, was aiding and abetting him in committing the crime.

A man may aid and abet to commit a crime, and yet do so quite innocently, not knowing that he was doing anything of the sort. He might do something which was essential to the principal for the execution of the crime, and yet he might do that in the ordinary course, and without any consciousness that he was aiding in the offence. On the other hand, it is not necessary to prove on a charge of aiding and abetting that there was any deliberate communication or concert between the principal offender and the man who is charged with aiding, because if you have a deliberate purpose to assist, if you do something which you know will assist the principal in committing his offence, and you know that he is engaged in committing his offence, then your charge of aiding and abetting would be made out. Here, again, in the case of Mr. Morland you must be satisfied that the statement which he signed was false to his knowledge and was published by him

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—that is the result of signing it, because he signed the certificate with the intention of publishing it—with knowledge of its falsity, and appreciation of its falsity, and with the intention that it should deceive shareholders. Here, again, in the first and second counts of the case of Lord Kylsant and the case of Mr. Morland we are only concerned with the deceit practised against the shareholders and not against any one else. There are many differences, of course, between Mr. Morland's position, on any view, and that of Lord Kylsant. Mr. Morland, as the accountant and auditor of the company, had the accounts put before him, but not until they had passed the court of directors. He had nothing to do with the preparation of the accounts; he had nothing to do with the general policy of the company; he had no knowledge, except incidentally, perhaps, of the Meat Transport Company, of the subsidiary companies, or of their position. All he knew was about the dividends which from time to time he had to deal with in the accounts as representing the profits coming from those companies. He had, so far as can be seen, no motive at all for any deceitful intention, unless possibly it may be said he was too pliant with the wishes of those in authority, but unless that is to be treated as motive I do not see any motive at all. Of course, it may be said against him that he did in fact add the sanction of his name as auditor to a document which, taking those two years 1926 and 1927, was false and misleading.

As I pointed out in another connection, it is not here a question of whether or not he did something less than would be expected as the full duty of a careful and conscientious auditor. It is the business of the auditor to certify, after proper examination, if he can honestly and according to his skill and understanding, that the accounts of the company present a true and correct view of the state of the company's affairs, and to the extent that he is not satisfied that he can properly give that certificate his duty is either to qualify the certificate or to ask to have the accounts altered in such a way that he can sign them without qualification. In the case of Mr. Morland, it is obvious enough that in the year 1926, when the accounts of 1925 were being dealt with, he was not satisfied with the position, because he thought that some words ought to be added to intimate to the shareholders that the moneys which we know were being used were being used in order to produce the balance which appears. That being so, he thought, as indeed he has admitted, that without some qualification or another he ought not to give the certificate, and the qualification which he suggested, and which he put in, was those words, which you must all be tired of hearing, "Adjustment of taxation reserves"—those words which Lord Plender has turned into plain English in the way in which I have already said. Mr. Morland says that that satisfied his doubts; he thought then that he had done enough to cure the defective character of the balance sheet or profit and loss account with those words. If he was right in that, if he had discharged his duty sufficiently and properly, then it seems, on any view, that the matter is, or ought to be, at an end. If, on the other hand, he was wrong

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in this sense that in a civil action, or in an action against him for not showing due care and skill, he would be held liable as a defendant because he had broken his duty and not fully discharged his office, then, again, his liability would be a civil liability in damages. That is assuming against him that he ought to have done something else before he signed the certificate, that he ought to have taken some drastic step and some more effective step in order to bring to the minds of the shareholders the true position of the company's affairs; and it may well be that he did not discharge his duty efficiently and properly. It may well be that an auditor placed in his position, as, I venture to suggest, of a quasi-judicial character, standing between the directors and the shareholders, and protecting the interests of the shareholders against any possibility of their being misled by the directors—it may well be that he took an imperfect view, an inadequate view, of the very grave duties which rest upon auditors.

The profession of accountancy, as we know, is a very distinguished, very honourable, and a very essential profession in the commercial affairs of this country. Great trust must be reposed on the skill and judgment and honour of accountants. It may be that through error of judgment they fail to do all that the requirements of that high office demand. But, again, you are not concerned here with any question of civil liability or breach of duty. What you are concerned with, and what you have to determine, is whether there was, assuming that Lord Kylsant was guilty of this offence, a deliberate and conscious act on the part of Mr. Morland to help Lord Kylsant in carrying out that design by putting his hand to a certificate which he knew was not justified by the facts which he knew, and did not correspond with his duty; because, though the certificate stated in very clear terms that the accounts gave a true and correct view of the state of the company's affairs, he knew that they did not, and intended to give them currency and validity by means of his certificate with the knowledge that they did not give a true and correct view, and that he did so with a criminal and a wicked intent.

You have heard the evidence. He has called certain accountants whom you have heard. Three accountants have said in the witness-box that they would have signed the certificate in the same form—I suppose they would say under the same circumstances as Mr. Morland. That may be so or not, I do not know, but that is what they say, and I am sure that is what they believe at this moment. Of course, that does not relieve you of the duty of deciding as a preliminary step, whether it was a certificate that he ought to sign, or that he should sign in that form if he really appreciated his duty. As I have already pointed out, in such a way as almost to weary you, even if you come to that conclusion, you still have to decide on the question of the fraudulent and criminal intent, which is the third step you have to consider. If you think that he only committed an error of judgment, and something which fell short of his duty, you have still to consider, before you consider the question of intent at all, did he appreciate that he was doing wrong, or did he honestly believe that he had

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discharged his duty, however erroneous that belief was? Did he honestly believe he had discharged his duty by putting into the balance sheet in that and subsequent years those mystic words which are said to be so clear, but which may or may not be clear, "Adjustment of taxation reserves"? Supposing he honestly thought that that was enough, then, on any view of the case you could not find him guilty of fraudulent intent. However mistaken a man may have been, and however unfortunate the circumstances of his mistake may be, that does not constitute criminal intent or a criminal offence.

I have looked carefully through Mr. Morland's evidence. Probably you will remember the general substance of it, and I do not think that I can help you by going through it again. He does not dispute, nor, indeed, could he dispute, that he was dissatisfied with the accounts for 1925 in the form in which they were presented. He says: "I thought it desirable. I do not think I can put it higher than that," because his view is that you ought not to go on taking those large sums of money to swell the balance and do it for so long without intimating that to the shareholders. He thought he had done enough. You may think he had not done enough, but if you think that he honestly believed he had done enough, then, apart from anything else, that ends the matter. I am not going back on what I said before; I shall simply leave the matter there with you, reminding you again, as I have reminded you on each previous matter, that in a criminal Court the jury have to be satisfied beyond reasonable doubt of the guilt of the person who is charged. That is a cardinal rule of British justice. In a Court of Law the jury cannot cast their eyes outside on other considerations. Their duty is to decide truly and indifferently, according to the evidence, with no other consideration than to decide justly according to their skill and understanding of the evidence before them; and, bearing that in mind, bearing in mind what I have said more than once, you will proceed to your duty. If you are satisfied beyond all reasonable doubt of the guilt of either of the defendants on any one or more of these counts, you will not be deterred by considering the consequences, the very serious consequences, which must follow from your verdict. That will not deter you from your duty.

A jury, in a grave matter of this sort, have a very serious responsibility, which must be of the utmost importance in the affairs of the country, and in the commerce of the nation. But, again, although that is so, though you must not shrink from doing what you think is right and proper, still you must be satisfied, in the sense I have indicated so often, before you come to any verdict against either of these defendants in this case. Now, will you consider your verdict?

The jury retired at 3.33 p.m., and at 5.18 p.m. a note was sent to the Judge.

Mr. JUSTICE WRIGHT—I have received a note from the jury, and I want to read it in the presence of those concerned, to know whether I require the presence of the jury. The jury wish to be instructed with

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regard to Counts 1 and 2. "With intent to deceive the said shareholders." They desire to know if the intent must be a fraudulent intent to justify a verdict of guilty. They cannot visualise an intent to deceive without being fraudulent. I think I shall require the jury to come back into the box.

At 5.20 p.m. the jury returned into the Court.

Mr. JUSTICE WRIGHT—Members of the jury, I have received a note from you, and, in order to answer it, and indeed in order to read it, it has been necessary, because the rule is very strict, that it should be done in open Court. You quite appreciate why it should be so, and, that being so, the question you ask in referring to the words in the indictment: "With intent to deceive the said shareholders", you ask whether the intent must be fraudulent, and then you add you "cannot visualise an attempt to deceive without it being fraudulent." Neither can I. The intent must be fraudulent, the essence of the offence is a fraudulent intent to deceive. You cannot intend to deceive unless you have fraud in your mind. The two things really are different ways of expressing the same thing, or rather the word "fraud" is a most compendious way of expressing "an attempt to deceive." Indeed, I notice in my copy of the Act—I have not got the actual Act, but I take it from Archbold, which is a sort of standard work which we always use in these Courts—section 84 has a sort of rubric or head note or side note, and this is what it is: "Publishing Fraudulent Statements," and then it goes on: "Whosoever being a director, manager or public officer of any body corporate or public company, shall make, circulate or publish or concur in making, circulating or publishing any written statement or account which he shall know to be false in any material particular, with intent to deceive or defraud"—to deceive or defraud any man, shareholder or creditor. The essence of that section is that the statement should be fraudulent, and various expressions are merely ways of defining the particular fraud which the section contemplates; therefore, the answer to your question is that the intent must be fraudulent; the answer, in the language which I believe is used in other places, is in the affirmative. Does that answer your question, members of the jury?

The FOREMAN OF THE JURY—Yes, my lord.

The jury again retired at 5.25 p.m., and were recalled into Court at 5.55 p.m.

Mr. JUSTICE WRIGHT—Members of the jury, I am very sorry to have to trouble you again, but it is so important that there should be no shadow of possibility of any confusion. In reading your letter I read these words: "They cannot visualise an intent to deceive without being fraudulent." I should have read these words: "They can visualise an intent to deceive without being fraudulent." The question was "With regard to Counts Nos. 1 and 2 of the indictment, 'with intent to deceive the said shareholders,'" and your letter goes on:

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"They desire to know if the intent must be a fraudulent intent to justify a verdict of guilty," and to that I said "Yes"; in my judgment, the intent to deceive must be fraudulent under the statute, and that in my judgment is the true meaning of this section. An intent to deceive, in my judgment, necessarily involves a fraudulent intent, because fraud involves an intent to deceive, and, therefore, the two things for this purpose may be treated as two terms, two expressions, and for this purpose may be treated as synonymous, meaning the same thing. An intent to deceive in my judgment involves fraudulent intent. Have I made it quite plain?

The FOREMAN—Yes

Sir JOHN SIMON—I do not know whether your lordship would be good enough to make plain that with regard to Counts 1 and 2 the jury must apprehend that they must consider the section as a whole.

Mr. JUSTICE WRIGHT—Yes; you understand that, members of the jury. You asked me about Counts 1 and 2, and I thought it right to deal with your question, but the answer is obviously the same with regard to the third count

Mr. PRITT—With regard to the third count it is "an attempt to induce" in the same way as the other

Mr. JUSTICE WRIGHT—Quite.

Mr. PRITT—But the actual intent as put by the section is an intent to induce.

Mr. JUSTICE WRIGHT—Yes, but I think, as regards the essence of the section, these rubrics and side notes have not the same effect as the Act, but the section is dealing with fraudulent statements. The third count follows the words of the same section, which again has reference to a fraudulent intent

The jury again retired at 6 p.m. and returned into Court at 6.33 p.m.

The CLERK OF THE COURT—Members of the jury, are you agreed upon your verdict.

The FOREMAN OF THE JURY—Yes.

The CLERK OF THE COURT—Do you find the prisoner Owen Coshy Philipps, Baron Kysant, guilty or not guilty?

The FOREMAN—On Counts Nos. 1 and 2, not guilty, and on Count 3, guilty.

The CLERK OF THE COURT—Do you find the prisoner Harold John Morland guilty or not guilty?

The FOREMAN—Not guilty.

The CLERK OF THE COURT—You find the prisoners not guilty on the first two counts, and you find Baron Kysant guilty on the third count, and that is the verdict of you all?

The FOREMAN—Yes.

Mr. JUSTICE WRIGHT—Mr Morland can be discharged. Sir John do you desire to say anything?

Sir JOHN SIMON—I have an application to make with reference to the Court of Criminal Appeal, but I do not desire to make it now.

## Sentence.

### SENTENCE.

Mr. JUSTICE WRIGHT—Lord Kysant, the jury have found you guilty on the third count of this indictment, which charges you with making, circulating, or publishing a written statement, namely, a prospectus, inviting the public to subscribe to an issue of debenture stock in the Royal Mail Steam Packet Company which you knew to be false in a material particular in that you concealed the true position of the company, with intent to induce people to entrust or advance property to the said company. You have held very high positions and have had an honourable career; but the offence of which you have been found guilty is one which cannot be regarded as other than very grave and very serious, especially in a commercial community, and especially having regard to the fact that it was committed with reference to a prospectus on which members of the public were invited to subscribe their money. I do not wish to say anything further. It is my duty in circumstances of this sort to decide and to state what I consider the appropriate sentence, because some sentence I must pass as in duty bound for an offence of this sort by whomsoever committed. I feel that I ought to take the most lenient view possible in view of your past career; and indeed any sentence I pass may be the least part of the punishment which may befall you. The sentence of the Court is that you be kept in prison, in the second division, for twelve months.

(*To the Jury*)—Members of the jury, you have had a very trying and arduous duty in this very long case, and under the circumstances I desire to recommend that you be excused from further attendance on any jury service for a period of ten years. That is the only form of compensation which it is in my power to give you.

Sir JOHN SIMON intimated that an appeal would be lodged, and suggested that Lord Kysant should be released on bail.

HIS LORDSHIP replied that he had been told that it was not a matter within his jurisdiction. A judge would be sitting in the High Court the following day, who could deal with the application. It was most unusual, although not unprecedented, for bail to be granted under such circumstances.

Sir JOHN SIMON said that application would be made elsewhere the following day, and added that the appeal would relate to the very important question of the construction of the section. That was a question of law. No leave to appeal was, therefore, required. He asked the judge, however, to grant him a certificate which he would need if he raised matters which might be regarded as both law and fact.

The JUDGE replied that it had not been his practice to grant certificates, and suggested that the application should be renewed before him the following morning in the High Court.





# APPENDICES.



# Appendix I.

## APPENDIX I.

### LORD KYLSANT'S APPEAL.

The appeal of Lord Kysant against the conviction and sentence of twelve months' imprisonment in the second division was heard in the Court of Criminal Appeal on the 2nd November, 1931. Lord Kysant had been on bail since 31st July. The hearing of the appeal occupied three days.

The appeal was heard by Mr Justice Avory, Mr. Justice Branson, and Mr Justice Humphreys. Lord Kysant appealed against the conviction and applied for leave to appeal against sentence.

The Attorney-General (Sir William Jowitt, K C ), Mr D. N Pritt, K C., and Mr. Eustace Fulton appeared for the Crown. Sir John Simon, K C, Mr J E Singleton, K.C., and Mr Wilfrid Lewis represented Lord Kysant.

Sir JOHN SIMON, in opening the appeal, criticised the framing of the indictment. The defence had called attention to the fact that it was in more general form than was usual, and had protested that they should know with more precision the nature of the falsity alleged. The crucial question, he contended, was that concerning the construction of section 84 of the Larceny Act, 1861. To this he directed a large part of his argument.

The grounds of the appeal were—

- (1) That there was no evidence that the appellant made or published, or concurred in making or publishing, a written statement which was false in any material particular.
- (2) That there was no evidence that he made or published the prospectus knowing it to be false in any material particular.
- (3) That there was no evidence that he made or published a prospectus which he knew to be false in a material particular with intent to induce persons to entrust or advance property to the Royal Mail Steam Packet Company; and
- (4) That the Judge at the trial had misdirected the jury.

Sir John Simon maintained that the question was whether the document was one which contained a statement known to be false. The real test, he apprehended, was: "Is that which is said to have been omitted deliberately omitted and of such a character that if it were added the words that are used are shown to be false?"

He suggested that if that were the true test, after the verdict of the jury on the first and second (i.e., the balance sheet) counts, there was no justification for the verdict on the third (i.e., the prospectus) count. The question was not whether there was not some material which some one might want to consider. It was whether the thing which had been omitted, if one imagined it to be added, made that which was affirmatively stated a lie.

Only upon a misconstruction of section 84, Sir John Simon argued, was there ground upon which his client ought to be convicted. The proposition to be found

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more than once in the summing-up to the jury was that section 84 set up a standard of communication, and said, for example, that there must be communicated to the shareholders or subscribers anything which it might be material for them to know; but he submitted that this was quite wrong. It might arise in some case in a Civil Court, but the proposition that the criminality of the publication of a prospectus could be judged by examining it for anything that was omitted which somebody might like to have been told was quite wrong. The Court, he believed, would not take the view that section 84 called for a complete disclosure of everything. In his summing-up Mr Justice Wright, counsel contended, had not made this clear to the jury.

The principal point of Sir John Simon's appeal was that "the only omissions which it is material to consider, and the only omission which section 84 of the Larceny Act of 1861 renders punishable, are omissions which added to what is stated make a false statement of the whole, and make what is stated false." This point alone occupied him for five hours.

In reply the ATTORNEY-GENERAL said that in his speeches to the jury he had made it plain, as had also Mr Justice Wright, what was meant by the use of the word "false," namely, that by stating some things and omitting others a false impression was created. He believed the test to be this: "Can you say that that which is stated creates one impression when if you had stated the other facts you would have completely removed the impression which you caused to be created?"

The prospectus, he argued, comprised not merely the fact stated in each sentence, but the inference and impression which any reasonable person obtained from reading the sentences and taking them as a whole. Any one looking at the prospectus, he urged, must have thought that the company was one in which they could fairly safely invest money, and he submitted that what was said, in the absence of what was omitted, created a false impression as to the true nature of the company. If that were so, the jury was perfectly entitled to come to the conclusion that the prospectus was a false document.

In his closing speech, Sir JOHN SIMON said he did not regard the prospectus as a highly satisfactory one. A law had since come into operation, the Companies Act of 1929, requiring that prospectuses should contain positive statements as to past profits, but that new law did not affect the case under consideration. While that most painful inquiry had called specific attention to the desirability of giving more information—and nothing he had argued was intended to suggest the contrary—on the law as it stood at the time, he submitted, although his client might have been too sanguine, he was never guilty of a fraudulent or false statement.

Mr. JUSTICE AVORY, in delivering judgment, said that the third ground of appeal was immaterial, because it was now admitted that if the prospectus was published and was false and known to be false there could be no doubt it was published with intent to induce persons to entrust or advance property to the company. Mr. Justice Avory referred to one or two authorities which, in the view of the Court, supported the view of the law expressed by Mr. Justice Wright.

In *Gluckstein v. Barnes*, reported in 1900 Appeal Cases, page 250, Lord Macnaghten said, giving his opinion in that case which concerned the company and its prospectus: "It is a trite observation that every document as against its author must be read in the sense which it was intended to convey. And

## Appendix I.

everybody knows that sometimes half the truth is no better than a downright falsehood "

In the case of *Peek v Gurney*, reported in six English and Irish appeals, Lord Chelmsford in giving his opinion in the House of Lords, that being a case where the House was considering the effect of the prospectus of a company which was formed to take over the business of Overend & Gurney, said : " It cannot be denied that if the condition of the firm of Overend & Gurney had been disclosed, the result must have been their stoppage, and no hope could have been entertained of establishing a joint stock company upon the basis of a concern in such a state. The foundation of the projected company was therefore necessarily laid in concealment; and to render the scheme attractive to the public the promoters were not only concerned to hide the scheme, but to give such a colour to the statements put forth in the prospectus as to render them (though perhaps literally true), yet, in the sense in which they must have known the statements would be understood by the public, really false."

In the latter case, Lord Cairns, giving his opinion, said . " This brings me, therefore, to the consideration of the prospectus, and before looking at the terms of it I may say that I entirely agree with what has been stated by my noble and learned friends before me, that mere silence could not, in my opinion, be a sufficient foundation for this proceeding. Mere non-disclosure of material facts, however morally censurable, however that non-disclosure might be a ground in a proper proceeding at a proper time for setting aside an allotment or a purchase of shares, would, in my opinion, form no ground for an action in the nature of an action for misrepresentation. There must, in my opinion, be some active misstatement of fact, or at all events such a partial and fragmentary statement of facts as that the withholding of that which is not stated makes that which is stated absolutely false "

They came to the case which was quoted by the Attorney-General in his opening, *Aaron's Reefs v. Turiss*, reported in 1896 Appeal Cases, in which Lord Halsbury, in giving his opinion, said this, on page 281 : " Inasmuch as the jury have found that, I think, upon very good evidence in the prospectus itself, it remains only to consider the final question, namely, whether or not there was evidence to the jury which would justify them in finding that this was a fraudulent prospectus; that these statements were fraudulent and false.

" Now, in dealing with that question again, I say I protest against being called on only to look at some specific allegation in it; I think one is entitled to look at the whole document and see what it means taken together. Now if you look at the whole document taken together, knowing what we now know and what the jury had before them, I suppose nobody can doubt that this was a fraudulent conspiracy. I observe that one or two of the learned judges below used very plain language upon it, and remarked upon the fact that Mr. Gilbert, who seems to have been the head and front of it, was not subjected to an inquiry in a Criminal Court. But be that as it may, the question before your lordships now is whether the jury were justified in finding with these facts before them what they did find.

" It is said there is no specific allegation of fact which is proved to be false. Again I protest, as I have said, against that being the true test. I should say, taking the whole thing together, was there false representation? I do not care by what means it is conveyed; by what trick or device or ambiguous language: all those are expedients by which fraudulent people seem to think

## The Royal Mail Case.

they can escape from the real substance of the transaction. If by a number of statements you intentionally give a false impression and induce a person to act upon it, it is not the less false, although if one takes each statement by itself there may be a difficulty in showing that any specific statement is untrue. . . .

"The whole of this transaction seems to me to have been fraudulent to the last degree, and I entirely concur with those learned judges who, in very plain language, said that the persons engaged in this transaction were guilty of a fraudulent conspiracy and might have been indicted for it."

Mr Justice Avory added: "In our opinion, in the opinion of this Court, these authorities are sufficient to support the summing up of Mr. Justice Wright so far as it consisted of any direction on the question of law arising in this case.

"It is true that they are opinions expressed in civil proceedings, but we think they are none the less applicable in this case, particularly in view of the fact that in the last case Lord Halsbury had in mind and gave expression to his view as to the criminal as well as the civil liability

"In the present case we find that the Judge on more than one occasion specifically called the attention of the jury to the distinction they must bear in mind between a possible civil liability and a criminal liability, and in the opinion of this Court there was ample evidence upon which the jury could come to the conclusion that this document, the prospectus, was false in a material particular, in that it conveyed a false impression

"The falsity in this case consists in putting before intending investors, as material upon which they can exercise a judgment as to the existing position of the company, figures which apparently disclose the existing position, but in fact conceal it. In other words, the document implied that the company was in a sound financial position and that a prudent investor could safely invest in its debentures "

The further question was whether there was evidence upon which the jury could properly find that the appellant knew that this document was false. Mr Justice Avory said that if there was evidence that it was false in the particulars already indicated, there was ample evidence upon which the jury could find that the appellant knew of its falsity, knowing, as he did, the means by which the dividends had been paid

"In the result," concluded Mr Justice Avory, "we come without hesitation to the conclusion that in the summing-up, regarded as a whole, there was no misdirection, that there was ample evidence upon which the verdict of the jury can be supported, and that this appeal must be dismissed."

Mr. Singleton called attention to the fact that there was an appeal also against the sentence.

Mr. Justice Avory said the Court had considered that matter, but would hear anything that counsel had to say.

Mr. Singleton said he desired to add a word, though not on the express instructions of Lord Kysant, to whom the conviction was the great thing that mattered. The Court knew his age and had seen his record in public and private life. Lord Plender, in the course of his evidence, said that Lord Kysant had offered every possible facility from the time inquiries were set on foot. Sir William M'Lintock agreed that that was so. The debenture issue was in June, 1928. Thereafter the company paid a dividend which would have entitled Lord

# Appendix I.

Kylsant to draw a commission, but he did not draw it because he did not wish to do so.

After a short consultation between the three judges, Mr. Justice Avory observed that the Court could see no reason why the sentence passed on the appellant should be altered.

The appeal against the sentence was also dismissed

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## APPENDIX II.

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### PROCEEDINGS AT THE GUILDHALL

On Tuesday, 2nd June, 1931, OWEN COSBY PHILIPPS, BARON KYLSANT of CARMARTHEN, appeared at the Mansion House Police Court, sitting at the Guildhall, London, to answer summonses relating to the affairs of the Royal Mail Steam Packet Company, of which he was chairman

With him, Mr Harold John Morland, chartered accountant, formerly auditor for the company, was also summoned.

The first summons read—

That you in the City on the 11th day of May, 1927, being a director of a certain public company, to wit, the Royal Mail Steam Packet Company, did make, circulate, or publish, or concur in making, circulating, or publishing, a certain written statement of accounts, to wit, the annual report of the directors of the said company for the year 1926, and dated 11th May, 1927, which you knew to be false in a material particular with intent to deceive the shareholders of the said company contrary to section 84 of the Larceny Act, 1861.

The second summons against Lord Kyslant was exactly similar, with the exception that it referred to the annual report of the directors for the year 1927, and dated 9th May, 1928.

The summonses against Mr. Morland alleged that ". . . he did aid, abet, counsel, procure, or command" Lord Kyslant in the issue of the statement of accounts in each of the two years named.

When the case for the prosecution was opened, a further charge was made against Lord Kyslant.

. . . that on the 29th of June, 1928, being a director of the Royal Mail Steam Packet Company, he did make, circulate, or publish, or cause to be published, a certain written statement, namely, a prospectus, which he knew to be false in a material particular, with intent to induce persons to advance and invest money in the said company contrary to the Larceny Act.

The hearing was before the Lord Mayor. The case for the prosecution was opened by Mr. D. N. Pritt, K.C., for the Crown, who had with him Mr. Eustace Fulton and Mr. H. A. K. Morgan. Lord Kyslant was represented by Sir John Simon, K.C., M.P., Mr. Wilfrid Lewis, and Mr. J. E. Singleton, K.C. Mr. Morland was defended by Sir Patrick Hastings, K.C., Mr. Stuart Bevan, K.C., and Mr. C. J. Conway, K.C.

At the end of the first day the hearing was adjourned until Monday, 8th

## The Royal Mail Case.

June, 1931, when evidence was heard from Lord Plender and Sir William M'Lintock. Lord Plender's evidence was as to the appointment of Sir William M'Lintock to examine the affairs of the R.M.S.P. group. Sir John Simon and Sir Patrick Hastings, for the defence, objected that this evidence was inadmissible as not relevant to the charges, and after some discussion the Lord Mayor ruled that it should be withdrawn. A curious difficulty then arose. Both Sir John Simon and Sir Patrick Hastings wished to put questions to Lord Plender, but the Lord Mayor ruled that they could not do so when his evidence had been adjudged not relevant.

The hearing was resumed on the third day, 11th June, when Sir John Simon and Sir Patrick Hastings declared that in view of the ruling by the Lord Mayor that evidence as to the balance sheets of other companies could not be admitted—although evidence of the general practice of the accountancy profession would be admitted—they and those associated with them in the defence of Lord Kylsant and Mr. Morland would withdraw from the Court, Sir John's and Sir Patrick's juniors remaining as a matter of courtesy in case there was any point the Lord Mayor wished to raise during the hearing.

The hearing continued on Monday, 15th June (fourth day); Wednesday, 17th June (fifth day); Friday, 19th June (sixth day), and ended on Monday, 22nd June (seventh day).

Both defendants were committed for trial, each being allowed bail in his own recognisances of £5000.

In response to the statutory caution explaining that they could either give evidence or reserve their defence or make any statement before being committed for trial, both defendants addressed the Bench.

Lord Kylsant said—

I desire to state in answer to the charges that everything I have done has been done in the honest belief that it was for the welfare of the Royal Mail Steam Packet Company, and its associated shipping companies, of which I am chairman, and, therefore, I say I am not guilty on any of these charges. I have never published any false statement, nor have I ever attempted to deceive any one. Acting on the advice of my counsel, I do not propose to give any evidence in this Court nor to call any witnesses at this stage.

Mr. Morland said—

As I understand the character of the charge against me, I am accused as auditor of the Royal Mail Steam Packet Company of signing untrue accounts for the years 1926 and 1927. I am still of the opinion that these accounts were, as my report stated, true and correct in every particular, and that, therefore, I was carrying out my duty as auditor in signing them. That being so, I entirely repudiate the charge which has been brought against me, and, on the advice of my counsel, I reserve my defence.

The Lord Mayor, in granting bail, said—

I am sure both defendants desire to offer their defence in the higher Court. It has been a very painful case for me to deal with, but I had no alternative as Chief Magistrate of this City.

The proceedings on the last day of the hearing occupied the Court only twelve minutes.



# Appendix III.

## PROSPECTUS OF THE ROYAL MAIL STEAM PACKET COMPANY.

*No Underwriting Commission has been or will be paid on this Issue*

*The Subscription List will open on Tuesday, the 3rd July, 1928, and will close on or before Wednesday, the 4th July, 1928.*

## THE ROYAL MAIL STEAM PACKET COMPANY.

*(Incorporated by Royal Charter, 1839.)*

Capital Authorised by Royal Charter, £25,000,000.

Capital Issued and Fully Paid, . . . . .	£8,800,000
4½ per cent. Debenture Stock, .. . . .	1,400,000
5 per cent. Debenture Stock, .. . . .	3,100,000
(Not including present issue.)	
Reserve Fund, . . . . .	1,450,000
Insurance Fund, . . . . .	1,311,755

ISSUE OF

**£2,000,000**

Five per cent. Debenture Stock at the price of £92 10s. per cent.

Payable as follows :—

On Application, . . . . .	5 per cent.	Applications
„ Allotment, . . . . .	5 „	must be made
„ 25th July, 1928, . . . . .	22½ „	in multiples
„ 19th September, 1928, . . . . .	30 „	of £10.
„ 17th October, 1928, . . . . .	30 „	
		<u>92½ per cent.</u>

Payment in full may be made on allotment, under discount at the rate of five per cent per annum. Thereafter payment in full can be made at any time under discount at the same rate, as at the due date of the instalment following date of payment in full.

Scrip Certificates will be issued in exchange for Letters of Allotment as soon as practicable after allotment and will be exchanged for registered Debenture Stock Certificates after the date of payment of the final instalment.

# The Royal Mail Case.

The Stock will be issued in multiples of £10, and after registered Stock Certificates have been issued will be transferable in any amount not involving a fraction of £1.

Present Stockholders will receive preferential allotment if they apply on the special coloured form provided for the purpose

Interest will be payable half-yearly, on 1st January and 1st July. A first interest payment of £1 15s per cent. (less Income Tax) will be made on 1st January, 1929, after which the Stock will rank for interest equally with the existing five per cent Stock.

The Company may at any time redeem the whole or any part of the Stock at par on giving six calendar months' notice to the Stockholders, but otherwise the Stock becomes redeemable only when the security created by the undermentioned Trust Deeds becomes enforceable

This Stock forms part of an authorised issue of Stock, equal to the issued and paid-up Capital of the Company for the time being ranking subject to and immediately after the First Debenture Stock of the Company. The present issue of Stock will be secured by a Supplemental Trust Deed in favour of Trustees giving a charge by way of floating security upon the undertaking, property, and assets of the Company, including uncalled Capital, subject only to the charge thereon created by the Trust Deeds for securing the First Debenture Stock for the time being issued which is not to exceed two-thirds of the paid-up Capital for the time being of the Company. The Trust Deeds securing the Stock, of which the present issue forms part, contain a provision prohibiting the Company, except as mentioned below, from creating any general charge upon its undertaking or property or from issuing any Debentures or Debenture Stock, or creating any specific mortgage or charge upon any of its ships in priority to or *pari passu* with the Debenture Stock. The right is reserved to the Company of creating and issuing from time to time further Debenture Stock ranking *pari passu* with this Stock to a total amount (including the £3,100,000 now issued and outstanding and the present issue) not exceeding the issued and paid-up Capital for the time being of the Company. The right is also reserved to the Company from time to time to issue further First Debenture Stock, ranking in priority to the Second Debenture Stock to an amount (including the £1,400,000 already issued) not exceeding two-thirds of the paid-up Capital for the time being of the Company

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## PROSPECTUS.

The Company was established by Royal Charter in 1839, and its powers have been extended by subsequent Royal Charters granted in the years 1851, 1882, 1904, 1912, and 1920. Under the Charter of 1904 it is stipulated as a cardinal principle of the Company that it is to be and remain under British control.

The object of this issue is to provide additional Capital for the new Freehold Building, Royal Mail House, Leadenhall Street, London, E.C., and for the general purposes of the Company.

The Company has issued no Debenture Stock since November, 1914

The combined fleets of the Royal Mail Steam Packet Company and of the

## Appendix III.

Shipping Companies of which the Royal Mail Steam Packet Company holds all the Stock or Shares consist of 116 steam and motor ships, including new vessels under construction, with an approximate gross register tonnage of 798,454 tons, whilst the combined fleets of the other Shipping Companies closely associated with the Royal Mail Steam Packet Company, and in which it is largely interested, represent a further gross register tonnage of 1,963,515 tons, making an aggregate total of 2,761,969 gross register tons. Many of the ships are fitted with refrigerating machinery for the carriage of chilled and frozen meat and other perishable products.

The interest on the present issue of Debenture Stock will amount to £100,000 per annum.

Although this Company in common with other Shipping Companies has suffered from the depression in the shipping industry, the audited Accounts of the Company show that during the past ten years the average annual balance available (including profits of the Insurance Fund) after providing for depreciation and interest on existing Debenture Stocks, has been *sufficient to pay the interest on the present issue more than five times over*.

After providing for all taxation, depreciation of the fleet, &c, adding to the Reserves and payment of dividends on the Preference Stocks, the dividends on the Ordinary Stock during the last seventeen years have been as follows :—

Year ended 31st December, 1912,	6 per cent.
„ „ 1913, . . . . .	6 „
„ „ 1914, .. . . .	Nil.
„ „ 1915, . . . . .	6 per cent
„ „ 1916, . . . . .	7 „
„ „ 1917, ... . .	7 „
„ „ 1918, ... . .	7 „
„ „ 1919, . . . . .	8 „
„ „ 1920, . . . . .	7 „
„ „ 1921, . . . . .	6 „
„ „ 1922, .... .	6 „
„ „ 1923, ... . .	6 „
„ „ 1924, .. . . .	6 „
„ „ 1925, .... .	5 „
„ „ 1926, .. . . .	4 „
„ „ 1927, . . . . .	5 „

A brokerage of £1 per cent. will be paid by the Company to Bankers and Stockbrokers in respect of all allotments made to the public on application forms bearing their stamp.

Applications on the Form accompanying the Prospectus should be forwarded to the Bankers together with the deposit of Five per cent.

If no allotment be made, the deposit will be returned in full. Should a partial allotment only be made, the surplus deposit will be appropriated towards the amount due on allotment, and any balance will be returned. Interest at the rate of seven per cent. per annum will be charged on all overdue amounts. Failure to pay any instalment on Stock allotted when due will render the allotment liable to be cancelled and all previous payments made in respect thereof liable to forfeiture.

# The Royal Mail Case.

Copies of the Royal Charter granted to the Company in 1839, of the supplemental Royal Charters granted in 1851, 1904, 1912, and 1920, of the Trust Deeds securing the Debenture Stocks already issued, and of the draft supplemental Trust Deed to secure the present issue, may be seen between the hours of 11 a.m. and 4 p.m. at the Offices of the Company's Solicitors, Ashurst, Morris, Crisp & Co., 17 Throgmorton Avenue, London, E.C., on any day while the Subscription List remains open.

Prospectuses and Forms of Application may be obtained at the offices of the Company, Royal Mail House, Moorgate, and Atlantic House, Moorgate, London, E.C.; America House, Cockspur Street, London, S.W.; and at the offices of the Company in Southampton, Liverpool, Manchester, Birmingham, Cardiff, and Glasgow, or from the Bankers and Brokers of the Company

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## Trustees for the Five Per Cent. Debenture Stockholders.

THE DUKE OF ABERCORN, K.G., K.P.  
VISCOUNT ST. DAVID, G.B.E., P.C.

## Directors.

THE LORD KYLSANT, G.C.M.G. (*Chairman*)  
THE DUKE OF ABERCORN, K.G., K.P.  
JOHN WILLIAM CLARK.  
A NEVILLE LURBOCK  
THE RIGHT HON. SIR LESLIE SCOTT, K.C., M.P.  
THE LORD SUFFIELD

## Bankers.

BARCLAYS BANK, LIMITED, 54 Lombard Street, London, E.C., and Branches  
COUTTS & CO, 15 Lombard Street, London, E.C., and 440 Strand, London, W.C.  
NATIONAL PROVINCIAL BANK, LIMITED, 15 Bishopsgate, London, E.C., and Branches.

## Solicitors.

ASHURST, MORRIS, CRISP & CO, 17 Throgmorton Avenue, London, E.C.

## Brokers.

SNELL & SWAFFIELD, 5 Copthall Buildings, London, E.C.  
KINGSMILL & HOLLINGSWORTH, 31 Throgmorton Street, London, E.C.

## Auditor

H. J. MORLAND, F.C.A. (of Price, Waterhouse, & Co.), 3 Frederick's Place, London, E.C.

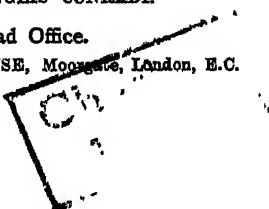
## Secretary.

DAVID INGLIS CONRAD.

## Head Office.

ROYAL MAIL HOUSE, Moorgate, London, E.C.

29th June, 1928.



**DETAILS OF PROFIT AND LOSS FROM 1920.**  
(EXHIBIT 21)

	1920		1921		1922		1923		1924		1925		1926		1927		1928		1929	
Gross Earnings of the Fleet, including Freight, Passage, Postal monies, Profits on Shops, &c.,	£9,825,689		£6,583,669		£4,882,322		£5,441,756		£ 479,188		£5,004,250		£5,798,251		£5,556,739		£5,051,428		£1,991,430	
Less Running Expenses,	7,532,075	£2,293,614	5,757,779	£325,890	4,072,451	£809,871	4,378,632	£1,063,124	517,144	£962,044	4,723,001	£880,349	4,882,486	£915,765	4,584,573	£972,166	4,304,268	£747,160	4,384,869	£609,561
Deduct—																				
General Administration,	£527,986		£585,194		549,566		£606,145		574,463		£597,120		£653,800		£590,158		£559,300		£531,166	
General Repairs and Maintenance,	815		7,426		9,082		4,259		5,372		1,652		4,504		2,246		—		—	
Insurance Fund,	439,325		426,200		195,742		192,243		139,025		167,369		162,322		211,300		153,179		112,681	
Depreciation of Fleet,	410,988		572,070		496,078		620,908		647,834		635,615		620,727		493,034		124,813		383,108	
Depreciation of Premises, Plant, &c.,	11,747		14,153		10,074		18,806		20,942		16,721		14,618		9,875		5,882		9,743	
Special Debits, enumerated below,	565,145	1,856,006	125,000	1,730,043	120,175	1,380,712	64,000	£1,506,361	75,851	1,463,487	—	1,450,486	—	1,455,971	—	1,306,013	19,768	802,542	18,000	1,054,698
Add—	Surplus,	£337,608	Deficit,	£904,163	Deficit,	£570,841	Deficit,	£443,237	Deficit,	£501,443	Deficit,	£570,137	Deficit,	£540,206	Deficit,	£334,447	Deficit,	£115,382	Deficit,	£445,137
Interest on Investments (Net),		500,045		452,101		435,477		422,351		404,272		261,032		267,965		559,354		452,728		385,205
Add—			Deficit,	£452,052	Deficit,	£135,364	Deficit,	£20,856	Deficit,	£97,171	Deficit,	£309,105	Deficit,	£372,241	Surplus,	£224,007	Surplus,	£337,346	Deficit,	£50,932
Special Credits, enumerated below,		£837,653		1,120,452		860,679		800,000		570,000		1,040,209		900,776		512,386		392,020		212,619
Surplus as per printed account		£837,653		£668,400		£725,315		£779,114		£772,829		£731,101		£628,538		£737,293		£729,368		£152,687
	Special Debits		Special Debit		Special Debits		Special Debits		Special Debits		Special Debits		Special Debits		Special Debits		Special Debit		Special Debit	
Excess Profits Duty,	£423,600		Excess Profits Duty,	£125,000	New Issue Expenses,	£55,443	Cancellation Fees Account, P S N Steamers,	£64,000	Loss on sale of "Orsa,"	£70,851	Compensation to Captain Findlay, Account, M Hotel,	£7,000					New Stock Expenses,	£19,768	New Stock Expenses,	£18,000
Corporation Profit Tax,	34,420				New York Service, Preliminary Expenses,	63,826			Cancellation of contract with Workman Clark & Co,	5,000	Cancellation of contract with Workman, Clark & Co, Ltd,	25,000								
New Issue Expenses,	77,125				U S A Income Tax,	906														
Premises Reserve,	80,000																			
	£565,145					£120,175				£75,851		£32,000								
	Special Credits		Special Credits		Special Credits		Special Credits		Special Credits		Special Credits		Special Credits		Special Credits		Special Credits		Special Credits	
Bonus Shares, Elder, Dempster & Co,	£80,812		Excess Profits Duty,	£100,000	Income Tax Reserve,	£450,000	Excess Profits Duty,	£380,000	Excess Profits Duty,	£380,000	Excess Profits Duty,	£300,000	Excess Profits Duty,	£550,000	Excess Profits Duty,	£232,788	Income Tax Reserve,	£350,000	Income Tax Reserve,	£123,007
Nelson Lane, Liverpool,	550,000		War Contingency Reserve,	45,060	Excess Profits Duty,	100,000	Income Tax Reserve,	350,000	Income Tax Reserve,	350,000	Income Tax Reserve,	250,000	Income Tax Reserve,	175,000	Income Tax Reserve,	120,000	Profit on Steamers and Premises sold,	17,020	Profit on Steamers and Premises sold,	89,012
Union Castle Co,	489,610		Profit on Sale of Steamers,	271,060	Deferred Repairs,	250,000	Deferred Repairs,	150,000	Deferred Repairs,	150,000	Investment Profit, Nelson Lane,	490,209	Investment Profit, Nelson Lane,	25,776	Investment Profit, Nelson Lane,	108,981	Premises Reserve,	10,000	Premises Reserve,	
			Fleet Depreciation Fund,	444,569					Corporation Profits Tax	40,000			Reserve Fund,	150,000	Corporation Profits Tax,	32,905	Wine Vaults Profit,	15,000		
															Sundry,	17,762				
				£1,120,452		£860,679		£800,000		£870,000		£1,040,209		£900,776		£512,386		£392,020		£212,619